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No. 84-95

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

NATIONAL ASSOCIATION OF
REGULATORY UTILITY COMMISSIONERS,
Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION AND
UNITED STATES OF AMERICA,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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QUESTION PRESENTED FOR REVIEW

Congress provided, in the express language of the Communications Act of 1934, that jurisdiction over telecommunications be divided between the federal government and the States. The Federal Communications Commission was granted authority over interstate and international communications, 47 U.S.C. sec. 151, while authority over the intrastate sphere was reserved to the States. 47 US.C. secs. 152(b), 221(b). Against this background, the questions presented are as follows:

1. Whether the decision of the District of Columbia Circuit affirming the FCC's end user access charge plan is consistent with this Court's decision in *Smith v. Illinois Bell* governing the regulatory treatment of local telephone company-owned facilities used for both interstate and intrastate communications?

2. Whether the Court of Appeals for the District of Columbia Circuit erred in concluding that the Federal Communications Commission acted within its statutory authority under the Communications Act of 1934 in promulgating its end user access charge plan?

PARTIES

The parties to the proceeding before the U.S. Court of Appeals for the District of Columbia Circuit are listed below.

Petitioners and intervenors supporting petitioners were as follows:

National Association of Regulatory Utility Commissioners;
Public Service Commission of the District of Columbia;
People of the State of California and the Public Utilities Commission of the State of California;
MCI Telecommunications Corporation;
Lexitel Corporation;
Wetern Union Telegraph Company;
North American Telecommunications Association;
Aeronautical Radio, Inc.;
United States Transmission Systems, Inc.;
Telesphere Network, Inc.;
Association of Long Distance Telephone Companies;
Iowa State Commerce Commission;
Washington Utilities and Transportation Commission;
Rural Telephone Coalition;
New York State Department of Public Service;
Roseville Telephone Company, et al.;
National Association of State Utility Consumer Advocates;
Maryland Office of People's Counsel;
Florida Public Service Commission;
Steven W. Hamm, as Consumer Advocate for the State of South Carolina;
Vermont Public Service Board;
Arizona Corporation Commission;
Public Service Commission of Wisconsin;
Public Service Commission of West Virginia;

State of Alaska, et al.;
Public Service Commission of Alabama;
Department of Public Utility Control of the State of Connecticut;
South Dakota Public Utilities Commission;
Missouri Public Service Commission;
State of Michigan, et al.;
American Petroleum Institute;
Association of Data Communications Users;
Utilities Telecommunications Council;
GTE Sprint Communications Corporation;
Satelco, Inc.;
Teletec Serving Communications Company;
U.S. Telephone, Inc.;
U.S. Transmission Systems, Inc.;
Tel Systems Management Corporation; and
GTE Service Corporation.

Respondents and intervenors supporting respondents were as follows:

Federal Communications Commission;
United States of America;
International Business Machines Corporation;
Bell System Operating Companies, et al.;
American Telephone & Telegraph Company;
MCI Telecommunications Corporation;
Rochester Telephone Corporation;
United States Telephone Association;
ROLM Corporation;
Ad Hoc Telecommunications Users Committee; and
Association of Data Processing Service Organizations.

The following parties were granted intervenor status but did not file briefs. Their positions are not known to petitioner:

Centel Corporation;
United Telephone Systems, Inc.;
American Broadcasting Companies, Inc.;
Illinois Commerce Commission;
Combined Network, Inc.;
Enhanced Communication Services Association; and
Allnet Communications Services, Inc.

Petitioner National Association of Regulatory Utility Commissioners (NARUC) is a quasi-governmental non-profit organization. Within its membership are the governmental agencies of the fifty States and of the District of Columbia, Puerto Rico and the Virgin Islands engaged in the regulation of carriers and utilities. More specifically, the members of the NARUC include the State officials responsible for ensuring the establishment and maintenance of such communications services and facilities as may be required by the public convenience and necessity and the furnishing of service at rates that are just and reasonable.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

The National Association of Regulatory Utility Commissioners (NARUC) petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit entered on June 12, 1984.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the District of Columbia Circuit is attached as Appendix A. The Federal Communications Commission's access charge order is reported at 93 FCC2d 241 (1983). Its order on initial reconsideration is reported at 48 Fed. Reg.

42,984 (1983). Its order on further reconsideration is reported at 49 Fed. Reg. 7,810 (1984).[1]

JURISDICTION

The decision of the District of Columbia Circuit was entered on June 12, 1984. This petition was filed within ninety days of that date. The jurisdiction of this Court is invoked under 28 U.S.C. sec. 1254(1).

STATUTES AND REGULATIONS

Relevant statutory provisions are set forth in Appendix B.

STATEMENT OF THE CASE

The genesis of the present controversy lies in the fact that facilities owned by local telephone companies,[2] which are subject to State utility commission regulatory authority, are used for both intrastate and interstate communications. All interstate telephone calls use both local telephone company property and interstate, long-distance facilities. The calls begin on a subscriber's local loop; they then travel through local telephone company switches to long-distance lines; from the long-distance lines, they drop back into the local system at the receiving end and pass in-

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[1]One complete set of the FCC's access charge orders, totaling approximately 500 pages, has been lodged with the Clerk of this Court today.

[2]Until recently, the 22 Bell Operating Companies (BOCs) were subsidiaries of AT&T. In 1982 the U.S. Justice Department and AT&T entered into a consent decree providing that AT&T would divest itself of the BOCs as of January 1, 1984. The BOCs, together with almost 1500 independent local companies, provide local telephone service.

to the call recipient's local loop. *NARUC v. FCC,* No. 83-1225, slip op. at 21 (D.C. Cir. June 12, 1984); Appendix A at 21.

At issue in this case is who should bear the costs of these local exchange facilities[3] and by what method these costs should be paid. Before 1930, in many jurisdictions, all local exchange plant costs were paid by local subscribers and were included in their local rates. Local telephone companies did not receive any reimbursement from AT&T[4] or long-distance customers for the origination and termination of their interstate calls.

However, this changed after 1930 when this Court decided *Smith v. Illinois Bell Telephone Company,* 282 U.S. 133 (1930). After *Smith* a portion of these costs were allocated to the interstate jurisdiction by a compromise measure which came to be known as the separations process. These allocated costs were then recovered by methods referred to as "settlements" and "division of revenues."[5] AT&T recovered NTS costs assigned to the interstate jurisdiction through usage-based charges imposed on the makers of long-distance calls. It then placed all interstate revenues into a "pool" and allocated a share of these revenues out of the pool to each local telephone company in proportion to its share of total interstate invest-

[3]Local exchange plant costs fall into two categories. Some of these costs are traffic sensitive (TS). They vary with usage. The remainder are non-traffic sensitive (NTS). These costs remain constant regardless of how many calls are made. We are concerned here only with the allocation and recovery of those costs that do not vary with usage (NTS costs).

[4]At this point in time AT&T was the monopoly long-distance carrier.

[5]"Settlements" refers to the method used by AT&T and the independent local telephone companies. "Division of revenues" refers to the method used within the AT&T corporate family.

ment. *NARUC v. FCC*, slip op. at 21-22 (D.C. Cir. June 12, 1984), Appendix A at 21-22. The basic "settlements" and "division of revenues" process was in effect when the FCC initiated the CC Docket No. 78-72 rulemaking proceeding at issue here.

Docket No. 78-72 originated in February 1978 with the issuance by the FCC of a *Notice of Inquiry and Proposed Rulemaking*, 67 FCC2d 757 (1978), designed to determine the MTS/WATS[6] market structure that would best serve the public interest. Until then, the FCC had followed policies premised on the notion that interstate MTS, WATS and equivalent services would be provided through franchised monopolies. In its *Third Supplemental Notice of Inquiry and Proposed Rulemaking*, 81 FCC2d 177 (1980) the FCC concluded that a general policy of open entry in the MTS/WATS market would be in the public interest. In light of this conclusion, the Commission determined that future proceedings in Docket No. 78-72 would be confined to a determination of how local telephone companies should be compensated for the use of their facilities to complete interstate communications.

In response to comments received on its tentative proposals, the FCC, on February 28, 1983, issued its *Third Report and Order*, 93 FCC2d 241 (1983) (*Access Charge Order)*. In this order the Commission stated that in deciding upon a compensation plan it sought to accommodate four potentially conflicting goals. The four objectives identified by the FCC were "the prevention of uneconomic

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[6]MTS is the FCC's name for standard long-distance telephone service. WATS provides a subscriber with access from his line to all phones in each of several geographic zones. 800 Service (formerly Inward WATS) enables him to receive long-distance telephone calls without the caller being charged. Outward WATS enables him to place long distance telephone calls for less than standard long-distance rates.

bypass;"[7] "the elimination of unjust discrimination or unlawful preferential rates;"[8] "the encouragement of network efficiency;" and "the continued assurance of universal service."[9] *Access Charge Order,* para. 122, 93 F.C.C.2d at 278. The FCC determined that its various goals could be accomplished best by moving toward a system in which virtually all NTS costs allocated to the interstate jurisdiction were recovered from end users through monthly flat-rate access charges.

The FCC has twice reconsidered its *Access Charge Order* and the compensation scheme embodied in that order. In its *Memorandum Opinion and Order on Reconsideration,* issued August 22, 1983, 47 Fed. Reg. 42,984 (*Reconsideration Order*), the FCC altered several aspects of its prior decision, including the level of end user access charges. In its *Memorandum Opinion and Order on Further Reconsideration,* issued February 15, 1984, 49 Fed. Reg. 7,810 (*Further Reconsideration Order*), the Commission again modified several important aspects of its prior scheme, including the level and timing of end user access charges. More specifically, the FCC deferred end user

[7]Bypass is the term used to describe what occurs when end users employ alternative technologies to take the place of the local exchange telephone system. The FCC feared and sought to avoid uneconomic bypass. Uneconomic bypass occurs when alternative technologies are cheaper to use only because use of the local exchange system is priced above cost. *NARUC v. FCC,* slip op. at 29 (D.C. Cir. June 12, 1984), Appendix A at 29.

[8]Section 202(a) of the Communications Act of 1934, 47 U.S.C. sec. 202(a), makes unlawful any "unjust or unreasonable discrimination in charges . . ." and "any undue or unreasonable preference or advantage to any particular person . . ."

[9]Section 151 of the Communications Act of 1934, 47 U.S.C. sec. 151, requires the FCC to "regulat[e] interstate . . . commerce in communication . . . so as to make available, so far as possible, to all people of the United States a rapid, efficient, Nationwide and worldwide . . . communication service with adequate facilities at reasonable charges."

charges for residential and single-line business customers until June 1985[10] and capped these charges at $4.00 per month through 1990.[11] However, the FCC throughout its reconsideration proceedings reaffirmed its conclusion that end user access charges should ultimately be imposed as the means to recover the bulk of NTS costs allocated to the interstate jurisdiction.

The NARUC filed its petition for review [Docket No. 83-1225] pursuant to 47 U.S.C. sec. 402(a) and 28 U.S.C. sec. 2342(i) in the U.S. Court of Appeals for the District of Columbia Circuit on March 1, 1983, after the FCC released its *Third Report and Order.* The Public Service Commission of the District of Columbia, [Docket No. 83-1329], the People of the State of California and the Public Utilities Commission of the State of California [Docket No. 83-1439], MCI Telecommunications Corp. [Docket No. 83-1463], Lexitel Corporation [Docket No. 83-1464], the Western Union Telegraph Company [Docket No. 83-1493] and the Association of Data Processing Service Organizations, Inc. [Docket No. 83-1505][12] all filed separate petitions for review. These cases were consolidated.

Subsequent to release by the FCC of its *Memorandum Opinion and Order on Reconsideration* Illinois Bell Telephone Company et al. [Docket No. 83-1912],[13] North

[10]Multi-line business access charges, beginning at $6.00 per month, remained unaltered by the FCC's reconsideration orders. These charges were implemented on May 25, 1984.

[11]The FCC has also instituted further decisionmaking on several matters: the amount of end user charges after 1990; exemptions from access charges for low income subscribers; the timing of increases in end user charges; and mechanisms to fulfill the particular needs of small telephone companies in high cost areas. *Further Reconsideration Order,* paras. 15-26, 49 Fed. Reg. 7,812-13.

[12]Pursuant to petitioner's motion this appeal was withdrawn by the Court on November 15, 1983.

[13]Pursuant to petitioner's motion this appeal was withdrawn by the Court on November 15, 1983.

American Telecommunications Association [Docket No. 83-1954], MCI Telecommunications Corp. [Docket No. 83-1984], the Public Service Commission of the District of Columbia [Docket No. 83-1995], Aeronautical Radio, Inc. [Docket No. 83-2016], Satellite Business Systems [Docket No. 83-2035], and United States Transmission Systems, Inc. [Docket No. 83-2108] filed petitions for review. These cases were consolidated with the consolidated cases under Docket No. 83-1225.

Before the D.C. Circuit, the NARUC argued *inter alia* that the FCC, in imposing flat-rate end user access charges which are a precondition to obtaining local service, violated the mandate of this Court in *Smith v. Illinois Bell.* The NARUC argued that *Smith* mandates that a portion of the costs of local exchange facilities must be both allocated to and recovered from the interstate jurisdiction. If, as is the case with the FCC's plan, end users must pay an interstate access charge as a precondition to obtaining local service, the access charge becomes an additional local rate which violates *Smith's* conclusion that these separated and allocated costs must be recovered from the interstate jurisdiction. The NARUC also asserted that because payment of the FCC's interstate end user access charge is a precondition to obtaining local service it amounts to a local charge which the FCC is without jurisdiction under the Communications Act of 1934 to impose.[14]

On June 12, 1984 the D.C. Circuit issued its decision affirming the FCC's access charge orders in all major re-

[14]A host of other issues relating to the FCC's interstate access charge plan but not relating to the end user access charge portion of that plan were raised by other petitioners and supporting intervenors. These issues are not germaine to the NARUC's petition and will not be discussed here.

spects including the issues raised by the NARUC relating to the FCC's end user access charges. *NARUC v. FCC*, No. 83-1225, slip op. at 19 (D.C. Cir. June 12, 1984), Appendix A at 19.

REASONS FOR GRANTING THE WRIT

a. The Decision of the U.S. Court of Appeals for the District of Columbia Circuit Conflicts With this Court's Decision in *Smith v. Illinois Bell*

The Communications Act of 1934, 47 U.S.C. sec. 151, grants the FCC jurisdiction to regulate interstate communications but mandates that regulation of the intrastate communications sphere be reserved to the States. Jurisdictional problems do arise, however, because many local facilities are used for both intrastate and interstate communications. In 1930 this Court addressed these problems in *Smith v. Illinois Bell Telephone Company*, 282 U.S. 133 (1930).

Before *Smith*, most local telephone companies did not receive any compensation from interstate carriers for originating and terminating their calls. For example, in the case of Illinois Bell Telephone Co. in the period prior to this Court's decision in *Smith v. Illinois Bell*, Illinois Bell owned and operated all the property in the city of Chicago used in intrastate communications and connected this property with the property owned by AT&T at the city limits to allow AT&T to provide long-distance service. In the method used by Illinois Bell, its local exchange property (property used at the subscribers station and from that station to the toll switchboard or to the toll trunk lines) was attributed entirely to the intrastate service and no portion was recovered from AT&T. This method, known as "board-to-board" ratemaking, was adopted for convenience

because of an inability to physically divide the property and was in use by a number of other State commissions at the time of the case. 282 U.S. at 150. *See Re Indiana Telephone Co.,* P.U.R. 1922C, 348 (Ind.); *Michigan State Telephone Co.,* P.U.R. 1923A, 30 (Mich.); *Re Northwestern Bell Telephone Co.,* P.U.R. 1922C, 762 (Minn.). The *Smith v. Illinois Bell* appellants attacked this procedure. They maintained that AT&T used, in its long-distance service, the local exchange plant of Illinois Bell without properly reimbursing Illinois Bell for this use. They advocated an alternative ratemaking theory called "station-to-station" ratemaking.

Station-to-station ratemaking apportions the costs of local exchange property between local and long-distance service. This ratemaking methodology is supported conceptually by the fact that all property from the originating to the terminating telephone station, as well as local switching, is used and necessary in order to complete long-distance calls.

In deciding the *Smith* case this Court clearly abandoned board-to-board ratemaking. The Court declared that it is "essential to the appropriate recognition of the competent governmental authority in each field of regulation" for there to be a separation of the interstate and intrastate property, revenues and expenses of a company. 282 U.S. at 148. The Court adopted the appellant's position and further held that, for the purposes of fixing just and reasonable rates for interstate and intrastate service, the local exchange carrier must be *reimbursed from within the interstate jurisdiction* for the use of his facilities by the long-distance carriers. This Court stated:

> While the difficulty in making an exact apportionment of the property is apparent, and ex-

> treme nicety is not required, only reasonable measures being essential, it is quite another matter to ignore altogether the actual uses to which the property is put. *It is obvious that unless an apportionment is made, the intrastate service to which the exchange property is allocated will bear an undue burden. . . .*
>
> *282 U.S. at 150-151*
> *(Citations Omitted, Emphasis Added)*

Smith was designed by this Court to prevent local exchange ratepayers from being unjustly straddled with all the costs of the local exchange network.

Faced with the problem of implementing the *Smith v. Illinois Bell* mandate, the telephone companies, State public utility commissions and federal agencies came to an agreement in the form of a "Separations Manual" standardizing allocations procedures. The Manual, which is published by the NARUC and approved by the FCC, has been revised and is incorporated into the FCC's rules, 47 C.F.R. sec. 67.1 (1979). *See Jurisdictional Separations of Telephone Companies,* 16 FCC2d 317, 331 (1969). In 1970, the Manual was revised pursuant to the "Ozark Plan," which was recommended by a Federal-State Joint Board convened under section 410(c) of the Communications Act, 47 U.S.C. sec. 410(c). *See Separations Procedures,* 26 FCC2d 247 (1970).[15]

[15]Section 410(c) of the Communications Act requires the FCC to refer to any rulemaking proceeding regarding the jurisdictional separation of property and expenses between the intrastate and interstate spheres to a Federal-State Joint Board for a recommended decision.

In its *Access Charge Order* the FCC acknowledged the applicability of *Smith v. Illinois Bell* and the necessity of allocating costs between the interstate and intrastate jurisdictions.[16] It stated that:

> It is the separations process that determines what costs must be recovered from the interstate jurisdiction. . . .

Access Charge Order, para. 13. Yet, the Commission went on to determine that *Smith* is not violated if an overwhelming majority of the NTS local exchange costs that are assigned to the interstate jurisdiction are ultimately recovered through flat per-line charges that are assessed upon all end users as a precondition to obtaining local service, *Id.* at para. 5, and it adopted access charge computation rules to accomplish that result.[17] Its interpretation was upheld by the U.S. Court of Appeals for the D.C. Circuit (D.C. Circuit).

The NARUC maintains that the interpretation placed on *Smith* by the FCC and ratified by the D.C. Circuit is incorrect. *Smith* necessitates the fulfillment of two criteria.

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[16]The Separations Manual generally allocates costs according to the relative use of facilities for intrastate and interstate services. The NTS costs at issue here do not, however, lend themselves to allocation on a usage basis. NTS costs are currently allocated on a usage/cost percentage basis. However, pursuant to a recent FCC decision the allocation of NTS costs will change beginning January 1, 1986. There will be a four-phase transition period which will result ultimately in a flat 25 percent allocation of NTS costs to the interstate jurisdiction. *Decision and Order,* CC Docket No. 80-286, 49 Fed. Reg. 7934 (March 2, 1984).

[17]Costs assigned to the interstate jurisdiction for customer premises equipment, inside wiring and a universal service fund are, however, to be recovered by charges on long-distance carriers under the FCC's decision. *Access Charge Order,* para. 5.

First, it requires that there be an allocation of jointly-used local exchange property between the interstate and intrastate jurisdictions based roughly on "the actual uses to which the property is put." 282 U.S. at 151. Second, *Smith* by its nature requires that the costs of the jointly-used local exchange property allocated to the interstate jurisdiction be recovered from within the interstate sphere, i.e., from interstate end users[18] or interstate carriers. Recovery from within the interstate sphere is necessary to fulfill this Court's requirement that local exchange ratepayers do not bear an undue burden.

The D.C. Circuit recognized, as had the FCC before it, the validity of the first criteria outlined above. The Court agreed that *Smith* mandates the allocation of some local exchange plant costs to the interstate jurisdiction. *NARUC v. FCC*, No. 83-1225, slip op. at 37, Appendix A at 37. The D.C. Circuit concluded, however, that *Smith's* mandate went no further. It adopted the position advanced by the FCC that the agency had exclusive authority to regulate the rates and rate structure through which the costs allocated to the interstate jurisdiction were to be recovered. The Court stated:

> The *Smith* Court did not address the manner in which the federal agency was to perform its task. It did not hold that the FCC must order recovery of costs allocated to its jurisdiction through usage-based charges.
>
> *NARUC v. FCC*, No. 83-1225, slip op. at 37-38, Appendix A at 37-38.

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[18]In *Smith* this Court made it clear that there exist two distinct classes of telephone ratepayers, those who use the intrastate system and those who use the interstate system. If interstate costs are to be recovered from end users they must be recovered from *interstate* end users.

The D.C. Circuit determined that once costs are allocated to the interstate jurisdiction *any* method adopted by the FCC to recover these costs is proper under *Smith*. This conclusion is incorrect. The NARUC agrees with the D.C. Circuit's conclusion that *Smith* does not specify the exact method by which these costs must be recovered. *Id.* at 37. It is true, as the Court specified, that recovery need not be on a usage-sensitive basis. It is also true that recovery need not necessarily be from long-distance carriers. What is true, however, is that recovery must come from within the interstate sphere. *Smith* would be stripped of all practical effect if this were not the case.

If the D.C. Circuit is correct and the FCC may recover these interstate costs from local exchange ratepayers, as it has attempted to do here, the result would be the same as if *Smith* had never been decided. Local exchange ratepayers would bear all the costs of the jointly-used local facilities, as they had before 1930. The economic burden *Smith* was purposefully designed to eradicate would remain in full force.

The D.C. Circuit concluded that the undue burden on local ratepayers which this Court sought to remedy in deciding *Smith* was only the burden which resulted when State utility commissions allowed local operating companies to include all local exchange plant costs in their rate bases. The D.C. Circuit saw this as an impermissible extension of State jurisdiction. It stated:

> The State commission [ ] must count some exchange plant as interstate to avoid retaining interstate property, but not interstate revenues, in its calculations. By including interstate property in its jurisdictional domain, the State commis-

> sion would artificially inflate the intrastate rate base, and hence intrastate charges.
>
> *NARUC v. FCC*, No. 83-1225, slip op. at 37, n. 18, Appendix A at 37, n. 18.

The error in the D.C. Circuit's position is that it fails to accept the converse as true. If it is impermissible to allow the States to call for recovery of all local exchange plant costs from intrastate ratepayers it must also be improper to allow the FCC to do what amounts to the same thing by transferring all costs allocated to the interstate jurisdiction back to the intrastate jurisdiction for recovery through flat-rate end user access charges.

The FCC's flat-rate end user access charge is to be assessed monthly on all end users on a per-line basis as a precondition to obtaining local service. The FCC describes the charge as being imposed for access to the interstate system. However, the FCC's access charge must be paid before a telephone subscriber can avail himself of the local telephone system. As such, the charge amounts to an increase in intrastate rates. As an additional intrastate charge it violates *Smith's* mandate that all costs allocated to the interstate jurisdiction through the separations process be recovered from within the interstate sphere.

Congress was cognizant of this Court's mandate in *Smith* when it enacted section 410(c) of the Communications Act of 1934, 47 U.S.C. sec. 410(c). In 1971 Congress added section 410(c) to the Act. Its purpose was to compel the FCC to refer all matters regarding the separation of jointly-used local exchange property to a Federal-State Joint Board for a recommended decision. That section reads in pertinent part as follows:

> The Commission shall refer any proceeding regarding the jurisdictional separation of proper-

> ty and expenses between the intrastate and interstate operations . . . to a Federal-State Joint Board. . .
>
> 47 U.S.C. sec. 410(c).

The legislative history of that section demonstrates a clear Congressional intent and understanding that any Joint Board created by sec. 410(c) would allocate costs to the interstate jurisdiction to be recovered in a way that would compensate the local system for the interstate system's use of its facilities. For instance, the Senate in reporting favorably upon the House bill (H.R. 7048) creating 410(c), stated in part as follows:

> Thus, in order for each jurisdiction effectively to exercise its authority, procedures are needed to apportion the costs for services under each jurisdiction.
>
> Separation of costs for each jurisdiction is not subject to precise definition. Nevertheless, the allocations of costs must be reasonable, *i.e.*, the rate base for each jurisdiction must have appropriate correlation to the different uses of the commonly used plant.
>
> S.Rep. No. 362, 92d Cong., 1st Sess. *reprinted* in 1971 U.S. Code Cong. & Ad. News 1511, 1512.

Further, the following language appeared in the Congressional Record during debate on S.1908, the companion bill to H.R. 7048:

> It is essential to the public interest that procedures for separating such plant and expenses be fair and equitable so that no unreasonable burden will be placed on either the interstate or intrastate users of the telephone service.
>
> 117 Cong. Rec. 15,980 (1971)

The D.C. Circuit concluded that petitioners below placed too much emphasis on the legislative history of sec. 410(c). The Court pointed out that when sec. 410(c) was enacted, NTS costs allocated to the interstate jurisdiction were being recovered through usage-based charges. It further opined that Senator Magnuson, the author of the above-quoted language, "may have been concerned with protecting the legitimate interests of the State commissions under that system" and that "nothing in the legislative history of sec. 410(c), however, convince[d it] that the section was meant to freeze in place for all time the 1971 system for recovery of costs." *NARUC v. FCC,* No. 83-1225, slip op. at 38 n. 19, Appendix A at 38, n. 19.

The D.C. Circuit's conclusion as to the intent behind Sen. Magnuson's words is pure speculation without any basis in fact. Further, and more importantly, its conclusion that Congress did not intend, in enacting sec. 410(c), to compel recovery of interstate NTS costs on a usage-sensitive basis is irrelevant. The NARUC does not assert that recovery must be on a usage-sensitive basis, any method (whether it be flat-rate, usage-sensitive or tapered) which calls for recovery of interstate-allocated costs from within the interstate jurisdiction is proper under *Smith*. Congress, in enacting sec. 410(c), codified *Smith*. By doing so, it legislatively endorsed the principle that the costs of jointly-used local exchange facilities must be recovered from the jurisdiction to which they have been assigned. The D.C. Circuit below improperly endorsed a violation by the FCC of this principle. Its action should not be allowed to stand.

b. This Case is of Critical National Importance Because of its Impact on the Ability of the States to Lawfully Regulate Intrastate Communications in the Public Interest.

Sections 2(b) and 221(b) of the Communications Act, 47 U.S.C. sec. 152(b), 221(b), explicitly restrict the FCC's power over the entire national telecommunications network by reserving to the States exclusive authority over the intrastate sphere.[19] The FCC's end user access charge plan impermissibly intrudes into this intrastate sphere and, in doing so, hampers the States severely in their attempts to lawfully regulate in the public interest.

As detailed in subsection a, *supra* at 8, the FCC's flat-rate end user access charge is to be assessed monthly on all end users on a per line basis as a precondition to obtaining local service. In the FCC's view, the charge is being imposed for interstate access. However, preconditioning local service on the payment of this charge makes this

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[19]Section 2(b) of the Act, 47 U.S.C. sec. 152(b), denies the FCC jurisdiction over:

> charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communications service by wire or radio of any carrier.

Section 221(b) of the Act, 47 U.S.C. sec. 221(b), provides that:

> [s]ubject to the provisions of section 301 of this title, nothing in this chapter shall be construed to apply, or to give the Commission jurisdiction, with respect to charges, classifications, practices, services, facilities, for or in connection with . . . exchange service . . . even though a portion of such exchange service constitutes interstate or foreign communication, in any case where such matters are subject to regulation by a State commission or by local governmental authority.

charge amount to an additional intrastate rate.[20] Subscribers must pay this charge if they wish to obtain or continue *intrastate* service regardless of their use of the *interstate* network. As such, the charge conflicts with the mandate of the Communications Act that authority over intrastate rates and charges be vested solely in the States.

The D.C. Circuit concluded that the decisions of the U.S. Court of Appeals for the Fourth Circuit in *North Carolina Utilities Commission v. FCC,* 537 F.2d 787 (4th Cir.), *cert. denied,* 429 U.S. 1027 (1976) ("*NCUC I*") and *North Carolina Utilities Commission v. FCC,* 522 F.2d 1036 (4th Cir.), *cert. denied,* 434 U.S. 874 (1977) ("*NCUC II*") and its decision in *Computer and Communications Industry Association v. FCC,* 693 F.2d 198 (D.C. Cir.), *cert. denied,* 103 S.Ct. 2109 (1983) ("*Computer II*") were proper precedent for upholding the FCC's end user access charges. The Court below stated its reasoning as follows:

> In *Computer II* the FCC asserted exclusive rate regulatory authority over CPE: we upheld its

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[20]The D.C. Circuit concluded that the FCC's access charge did not amount to an additional intrastate charge because the interstate costs recovered through the FCC's charge were "necessarily incurred for each subscriber by virtue of that subscriber's interconnection into the local network. . ." *NARUC v. FCC,* No. 83-1225, slip op. at 40, Appendix A at 40. Assuming, *arguendo,* that interstate costs are incurred by subscribres merely through their access to the interstate network, the FCC's charge still remains illegal for those subscribers who do not make any use of the interstate system and who, if given the choice, would choose to take intrastate-only access. At the very least, the FCC must be required to make available intrastate-only telephone service.

More importantly, the NARUC does not agree with the D.C. Circuit's conclusion that a user incurs intrastate costs merely by being provided with access to the interstate system regardless of whether he *ever* makes use of the system. Costs are incurred when a user accesses the system to originate and terminate interstate calls.

order, although the equipment in question is necessary to make local calls, and although some subscribers might use their CPE only to make local calls. Similarly, here, the FCC asserts authority to condition end user access to the local telephone plant on the end user's payment of plant costs in the FCC's interstate domain, although the plant in question is necessary to make local calls, and although some subscriber's [sic] might use it to only make local calls. In each case, the very same equipment is by its nature a key element of both interstate and intrastate calling.

NARUC v. FCC, No. 83-1225 slip op. at 42, Appendix A at 42.

The D.C. Circuit's analogy of the present case to the circumstances of the *NCUC* cases and *Computer II* is flawed. In each of those cases the court was confronted with the conflicting regulatory treatment of the FCC and the States relative to the use and continued regulatory tariffing of terminal equipment. Both the D.C. Circuit and the Fourth Circuit based their decisions approving FCC preemption of State regulation on the fact that the use of terminal equipment is not feasibly separable for regulatory purposes. For example, the D.C. Circuit in *Computer II* recognized that one cannot deregulate only a portion of an item of terminal equipment. *Computer II,* 693 F.2d at 215.

In contrast, what is involved here is not the deregulation of a piece of equipment subject to dual regulatory jurisdiction, but the proper ratemaking treatment of *separable* non-traffic sensitive *costs* which have been allocated to the interstate jurisdiction for recovery. The D.C. Circuit cannot seriously argue that these costs are inseparable (unlike the physical use of the equipment at issue in *NCUC I, NCUC II,* and *Computer II*) since these costs have been

separated for nearly 40 years in compliance with *Smith,* the Separations Manual and 47 U.S.C. sec. 410(c).

Since non-traffic sensitive costs of local exchange facilities *are* separable for regulatory purposes, *NCUC I & II* and *Computer II* cannot be relied upon as precedent for preemption by the FCC of State regulatory authority over these costs. The FCC's end user access charge, therefore, impermissibly intrudes into the sphere of jurisdiction Congress reserved to the States and impacts on their ability to regulate within this sphere in the public interest.

CONCLUSION

For all of the reasons set forth herein, Petitioner prays that a writ of certiorari be issued to the United States Court of Appeals for the District of Columbia Circuit.

Respectfully submitted,

WILLIAM PAUL RODGERS, JR.
General Counsel
(Counsel of Record)

CHARLES D. GRAY
Assistant General Counsel

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Regulatory Utility Commissioners
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DATED: July 18,1984

APPENDIX A

Notice: This opinion is subject to formal revision before publication in the Federal Reporter or U.S.App.D.C. Reports. Users are requested to notify the Clerk of any formal errors in order that corrections may be made before the bound volumes go to press.

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 83-1225

NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS, PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and UNITED STATES OF AMERICA, RESPONDENTS

AD HOC TELECOMMUNICATIONS USERS COMMITTEE,
IOWA STATE COMMERCE COMMISSION,
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,
ASSOCIATION OF DATA COMMUNICATIONS USERS,
UTILITIES TELECOMMUNICATIONS COUNCIL,
RURAL TELEPHONE COALITION,
UNITED STATES INDEPENDENT TELEPHONE ASSOCIATION,
ROCHESTER TELEPHONE CORPORATION,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
WESTERN UNION TELEGRAPH COMPANY,
AERONAUTICAL RADIO, INC.,
MCI TELECOMMUNICATIONS CORPORATION,

Bills of costs must be filed within 14 days after entry of judgment. The court looks with disfavor upon motions to file bills of costs out of time.

ASSOCIATION OF DATA PROCESSING SERVICE
ORGANIZATIONS, INC.,
CENTEL CORPORATION,
NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE,
AMERICAN TELEPHONE AND TELEGRAPH COMPANY,
UNITED TELEPHONE SYSTEM, INC.,
ROSEVILLE TELEPHONE COMPANY, et al.,
PUBLIC SERVICE COMMISSION OF THE
DISTRICT OF COLUMBIA,
SOUTHERN PACIFIC COMMUNICATIONS COMPANY,
NATIONAL ASSOCIATION OF STATE UTILITY
CONSUMER ADVOCATES,
AMERICAN BROADCASTING COMPANIES, INC.,
MARYLAND OFFICE OF PEOPLE'S COUNSEL,
FLORIDA PUBLIC SERVICE COMMISSION,
TELTEC SAVING COMMUNICATIONS COMPANY,
SATELCO INC.,
TEL SYSTEMS MANAGEMENT CORPORATION,
GTE SERVICE CORPORATION,
STEVEN W. HAMM, AS CONSUMER ADVOCATE
FOR THE STATE OF SOUTH CAROLINA,
VERMONT PUBLIC SERVICE BOARD,
ARIZONA CORPORATION COMMISSION,
PUBLIC SERVICE COMMISSION OF WISCONSIN,
ILLINOIS COMMERCE COMMISSION,
UNITED STATES TRANSMISSION SYSTEM, INC.,
U.S. TELEPHONE, INC.,
COMBINED NETWORK, INC.,
PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
STATE OF ALASKA, et al.,
NORTH AMERICAN TELEPHONE ASSOCIATION,
PUBLIC SERVICE COMMISSION OF ALABAMA,
DEPARTMENT OF PUBLIC UTILITY CONTROL
OF THE STATE OF CONNECTICUT,
SOUTH DAKOTA PUBLIC UTILITIES COMMISSION,
ENHANCED COMMUNICATIONS SERVICES ASSOCIATION,
ROLM CORPORATION, INTERVENORS

No. 83-1329

PUBLIC SERVICE COMMISSION OF THE
DISTRICT OF COLUMBIA, PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA, RESPONDENTS

UNITED TELEPHONE SYSTEM, INC.,
MCI TELECOMMUNICATIONS CORPORATION,
GTE SERVICE CORPORATION,
ASSOCIATION OF DATA PROCESSING SERVICE
ORGANIZATIONS, INC.,
WESTERN UNION TELEGRAPH COMPANY,
TYMNET, INC.,
SOUTHERN PACIFIC COMMUNICATIONS COMPANY,
AERONAUTICAL RADIO, INC.,
UTILITIES TELECOMMUNICATIONS COUNCIL,
ASSOCIATION OF DATA COMMUNICATIONS USERS,
AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,
MISSOURI PUBLIC SERVICE COMMISSION,
ROSEVILLE TELEPHONE COMPANY,
NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE,
FLORIDA PUBLIC SERVICE COMMISSION,
STATE OF MICHIGAN, et al.,
AMERICAN BROADCASTING COMPANIES, INC.,
AD HOC TELECOMMUNICATIONS USERS COMMITTEE,
RURAL TELEPHONE COALITION, et al.,
ILLINOIS COMMERCE COMMISSION,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
STATE OF ALASKA, et al.,
NORTH AMERICAN TELEPHONE ASSOCIATION,
SOUTH DAKOTA PUBLIC UTILITIES COMMISSION,
INTERVENORS

No. 83-1439

People of the State of California and the
Public Utilities Commission of the
State of California, petitioners

v.

Federal Communications Commission and
United States of America, respondents

Southern Pacific Communications Company,
MCI Telecommunications Corporation,
GTE Service Corporation,
Association of Data Processing Service
Organizations, Inc.,
Roseville Telephone Company, et al.,
Rural Telephone Coalition, et al.,
United Telephone System, Inc.,
Western Union Telegraph Company,
Aeronautical Radio, Inc.,
American Telephone and Telegraph Company, et al.,
Public Service Commission of the
District of Columbia,
American Broadcasting Companies, Inc., et al.,
Ad Hoc Telecommunications Users Committee,
Illinois Commerce Commission,
International Business Machines Corporation,
State of Alaska, et al.,
North American Telephone Association, intervenors

No. 83-1463

MCI Telecommunications Corporation, petitioner

v.

Federal Communications Commission and
United States of America, respondents

ROCHESTER TELEPHONE CORPORATION,
UNITED TELEPHONE SYSTEM, INC.,
WESTERN UNION TELEGRAPH COMPANY,
SOUTHERN PACIFIC COMMUNICATIONS COMPANY,
ROSEVILLE TELEPHONE COMPANY, et al.,
AERONAUTICAL RADIO, INC.,
AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,
AMERICAN BROADCASTING COMPANIES, INC., et al.,
AD HOC TELECOMMUNICATIONS USERS COMMITTEE,
CENTEL CORPORATION,
ILLINOIS COMMERCE COMMISSION,
RURAL TELEPHONE COALITION,
PUBLIC SERVICE COMMISSION OF THE
DISTRICT OF COLUMBIA,
GTE SERVICE CORPORATION,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
STATE OF ALASKA, et al.,
NORTH AMERICAN TELEPHONE ASSOCIATION, INTERVENORS

No. 83-1464

LEXITEL CORPORATION, PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA, RESPONDENTS

UNITED TELEPHONE SYSTEMS, INC.,
ROSEVILLE TELEPHONE COMPANY, et al.,
SOUTHERN PACIFIC COMMUNICATIONS COMPANY,
MCI TELECOMMUNICATIONS CORPORATION,
AD HOC TELECOMMUNICATIONS USERS COMMITTEE,
AMERICAN BROADCASTING COMPANIES, INC., et al.,
CENTEL CORPORATION,
ILLINOIS COMMERCE COMMISSION,
WESTERN UNION TELEGRAPH COMPANY,
ROCHESTER TELEPHONE CORPORATION,

Aeronautical Radio, Inc.,
Rural Telephone Coalition,
Public Service Commission of the
District of Columbia,
American Telephone and Telegraph Company, et al.,
GTE Service Corporation,
International Business Machines Corporation,
Vermont Public Service Board,
Public Service of the State of Vermont,
State of Alaska, et al.,
North American Telephone Association, intervenors

No. 83-1493

Western Union Telegraph Company, petitioner

v.

Federal Communications Commission and
United States of America, respondents

MCI Telecommunications Corporation,
Ad Hoc Telecommunications Users Committee,
American Broadcasting Companies, Inc.,
Southern Pacific Communications Company,
United Telephone System, Inc.,
Rochester Telephone Corporation,
Rural Telephone Coalition, et al.,
Aeronautical Radio, Inc.,
Public Service Commission of the
District of Columbia,
Roseville Telephone Company, et al.,
American Telephone and Telegraph Company, et al.,
GTE Service Corporation,
International Business Machines Corporation,
Public Service Commission of West Virginia,
State of Alaska, et al.,
North American Telephone Association, intervenors

No. 83-1954

NORTH AMERICAN TELEPHONE ASSOCIATION, PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA, RESPONDENTS

GTE SPRINT COMMUNICATIONS CORPORATION,
MCI TELECOMMUNICATIONS CORPORATION,
GTE SERVICE CORPORATION,
WESTERN UNION TELEGRAPH COMPANY,
ASSOCIATION OF DATA PROCESSING SERVICE
ORGANIZATIONS, INC.,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
BELL SYSTEM OPERATING COMPANIES, et al., INTERVENORS

No. 83-1984

MCI TELECOMMUNICATIONS CORPORATION, PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA, RESPONDENTS

GTE SERVICE CORPORATION,
WESTERN UNION TELEGRAPH COMPANY,
DEPARTMENT OF PUBLIC UTILITY CONTROL
OF THE STATE OF CONNECTICUT,
GTE SPRINT COMMUNICATIONS CORPORATION,
ASSOCIATION OF DATA PROCESSING
SERVICE ORGANIZATIONS,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
AMERICAN PETROLEUM INSTITUTE,
BELL SYSTEM OPERATING COMPANIES, et al., INTERVENORS

No. 83-1995

PUBLIC SERVICE COMMISSION OF THE
DISTRICT OF COLUMBIA, PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA, RESPONDENTS

GTE SPRINT COMMUNICATIONS CORPORATION,
GTE SERVICE CORPORATION,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
BELL SYSTEM OPERATING COMPANIES, et al.,
CENTEL CORPORATION, INTERVENORS

No. 83-2016

AERONAUTICAL RADIO, INC., PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA, RESPONDENTS

WESTERN UNION TELEGRAPH COMPANY,
GTE SPRINT COMMUNICATIONS CORPORATION,
ASSOCIATION OF DATA PROCESSING SERVICE
ORGANIZATIONS, INC.,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
GTE SERVICE CORPORATION,
MCI TELECOMMUNICATIONS CORPORATION,
BELL SYSTEM OPERATING COMPANIES, et al., INTERVENORS

No. 83-2108

UNITED STATES TRANSMISSION SYSTEMS, INC., PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA, RESPONDENTS

GTE SPRINT COMMUNICATIONS CORPORATION,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
GTE SERVICE CORPORATION,
MCI TELECOMMUNICATIONS CORPORATION,
BELL SYSTEM OPERATING COMPANIES, et al.,
NORTH AMERICAN TELEPHONE ASSOCIATION,
AERONAUTICAL RADIO, INC.,
WESTERN UNION TELEGRAPH COMPANY, INTERVENORS

No. 83-2168

TELESPHERE NETWORK, INC., PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA, RESPONDENTS

AMERICAN BROADCASTING COMPANIES,
AD HOC TELECOMMUNICATIONS USERS COMMITTEE,
AMERICAN TELEPHONE AND TELEGRAPH COMPANY,
BELL SYSTEM OPERATING COMPANIES,
NORTH AMERICAN TELEPHONE ASSOCIATION,
CENTEL CORPORATION,
ALLNET COMMUNICATION SERVICES, INC.,
MCI TELECOMMUNICATIONS CORPORATION,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
AERONAUTICAL RADIO, INC.,
GTE SERVICE CORPORATION,
ASSOCIATION OF DATA PROCESSING SERVICE
ORGANIZATIONS, INC., INTERVENORS

No. 83-2218

ASSOCIATION OF LONG DISTANCE TELEPHONE COMPANIES, PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA, RESPONDENTS

WESTERN UNION TELEGRAPH COMPANY,
AERONAUTICAL RADIO, INC.,
INTERNATIONAL BUSINESS MACHINES CORPORATION,
MCI TELECOMMUNICATIONS CORPORATION,
AMERICAN TELEPHONE AND TELEGRAPH COMPANY, et al.,
CENTEL CORPORATION,
NORTH AMERICAN TELEPHONE ASSOCIATION,
TELTEC SAVING COMMUNICATIONS COMPANY,
SATELCO INC.,
AD HOC TELECOMMUNICATIONS USERS COMMITTEE,
AMERICAN BROADCASTING COMPANIES, INC., et al.,
ALLNET COMMUNICATIONS SERVICES, INC.,
ROLM CORPORATION,
GTE SERVICE CORPORATION,
ASSOCIATION OF DATA PROCESSING SERVICE
ORGANIZATIONS, INC., INTERVENORS

Petitions for Review of Orders of the
Federal Communications Commission

Argued April 18, 1984 and April 19, 1984

Decided June 12, 1984

Genevieve Morelli, Deputy Assistant General Counsel, National Association of Regulatory Utility Commissioners, with whom *Paul Rodgers*, General Counsel, and *Charles D. Gray*, Assistant General Counsel, National Association of Regulatory Utility Commissioners, were on the brief, for National Association of Regulatory Utility Commissioners, petitioner in No. 83-1225. *Deborah A. DuPont*, Attorney, National Association of Regulatory Utility Commissioners, also entered an appearance for National Association of Regulatory Utility Commissioners.

William J. Byrnes, with whom *Michael H. Bader*, *Kenneth A. Cox*, *Joel Rothstein Wolfson*, *Theodore D. Kramer*, *Robert Michelson*, and *Robert E. Conn* were on the brief, for MCI Telecommunications Corp., petitioner in Nos. 83-1463 and 83-1984, and intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1464, 83-1493, 83-1954, 83-2016, 83-2035, 83-2108, 83-2168, and 83-2218.

John L. Bartlett, with whom *Robert J. Butler*, *Carl R. Frank*, *Richard E. Wiley*, *Philip V. Permut*, *Howard D. Polsky*, and *James M. Tobin* were on the brief, for Aeronautical Radio, Inc. and Lexitel Corp., petitioners in Nos. 83-1464 and 83-2016, and intervenors in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, 83-1493, 83-2108, 83-2168, and 83-2218.

Lloyd N. Moore, Jr., with whom *Howard C. Davenport* and *Michael E. Geltner* were on the brief, for Public Service Commission of the District of Columbia, petitioner in Nos. 83-1329 and 83-1995, and intervenor in Nos. 83-1225, 83-1439, 83-1463, 83-1464, and 83-1493.

Denise Bonn, with whom *Albert H. Kramer* was on the brief, for North American Telecommunications Association, petitioner in No. 83-1954 and intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, 83-1493, 83-2168, and 83-2218.

J. Calvin Simpson and *Peter G. Fairchild* were on the brief for People of the State of California, *et al.*, petitioners in No. 83-1439.

Arthur H. Simms, Lawrence P. Keller, Joel Yohalem, H. Richard Juhnke, Edward Berlin, Carmen D. Legato, and *Francis S. Blake* were on the brief for Western Union Telegraph Co., petitioner in No. 83-1493 and intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, 83-1954, 83-1984, 83-2016, 83-2035, 83-2108, and 83-2218.

Jeffrey H. Matsuura, F. Thomas Tuttle, William D. English, Kevin H. Cassidy, William E. Willis, Margaret K. Pfeiffer, Robert B. Bell, J. Laurent Scharff, and *Richard Singer* were on the brief for Satellite Business Systems, petitioner in No. 83-2035 and intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, and 83-1493.

John A. Ligon, Grant S. Lewis, and *John S. Kinzey* were on the brief for United States Transmission Systems, Inc., petitioner in No. 83-2108 and intervenor in No. 83-1225.

Leo I. George was on the statement in lieu of brief for Telesphere Network, Inc., petitioner in No. 83-2168.

Victor J. Toth was on the statement in lieu of brief for Association of Long Distance Telephone Companies, petitioner in No. 83-2218.

John E. Ingle, Counsel, Federal Communications Commission, with whom *Bruce E. Fein,* General Counsel, *Daniel M. Armstrong,* Associate General Counsel, *Nancy E. Stanley, Jane E. Mago,* and *Linda L. Oliver,* Counsel, Federal Communications Commission, were on the brief, for Federal Communications Commission, respondent in all cases.

Robert B. Nicholson, Frederic Freilicher, Barry Grossman, and *Nancy Garrison* were on the statement in lieu

of brief for United States of America, respondent in all cases.

Bruce Renard for Florida Public Service Commission, intervenor in Nos. 83-1225 and 83-1329.

Benjamin H. Dickens, Jr., with whom *Jack Shreve* for National Association of State Utility Consumer Advocates and *Joel B. Shifman* for Public Service Commission of West Virginia were on the joint brief, for National Association of State Utility Consumer Advocates, *et al.*, intervenors in Nos. 83-1225 and 83-1493. *Lee Jedziniak* also entered an appearance for Consumer Advocates of South Carolina.

Raymond F. Scully, with whom *Robert P. Casey* was on the brief, for Bell Operating Companies, intervenors in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, 83-1493, 83-1954, 83-1984, 83-1995, 83-2016, 83-2035, 83-2108, 83-2168, and 83-2218.

Michael Boudin, with whom *David H. Remes, Howard J. Trienens, Daniel Stark, Alfred A. Green*, and *Judith A. Maynes* were on the brief, for AT&T Co., intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, 83-1493, 83-1954, 83-1984, 83-1995, 83-2016, 83-2035, 83-2108, 83-2168, and 83-2218. *M. Jean Dabney, James D. Ellis, Alfred Winchell Whitaker*, and *Hiram D. Gordon* also entered appearances for AT&T Co.

Mary Jo Manning for ROLM Corporation, intervenor in Nos. 83-1225 and 83-2218.

Charles M. Meehan, with whom *Shirley S. Fujimato* for Utilities Telecommunications Council, *Deborah Shur Trinker, Lee M. Weiner*, for Association of Data Communications Users, *Wayne V. Black*, and *Stark Ritchie* for American Petroleum Institute, were on the joint brief, for American Petroleum Institute, *et al.*, intervenors in Nos. 83-1225, 83-1329, and 83-1984.

David Cosson, with whom *Amy S. Gross*, *Margot Smiley Humphrey*, and *Ellen S. Deutsche* were on the brief, for Rural Telephon Coalition, intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, and 83-1493.

J. Roger Wollenberg, *William T. Lake*, and *Roger M. Witten* were on the brief for International Business Machines Corp., intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, 83-1493, 83-1954, 83-1984, 83-1995, 83-2016, 83-2035, 83-2108, 83-2168, and 83-2218.

Joseph M. Kittner, *Randolph J. May*, and *Timothy J. Cooney* were on the brief for Ad Hoc Telecommunications Users Committee, intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, 83-1493, 83-2168, and 83-2218.

Herbert E. Marks, *Joseph P. Markoski*, *Judith Jurin Semo*, and *David A. Warmser* were on the brief for Association of Data Processing Service Organizations, Inc., intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1954, 83-1984, 83-2016, 83-2168, and 83-2218.

Richard E. Wiley, *Philip V. Permut*, *Danny E. Adams*, *Howard D. Polsky*, *Philip M. Walker*, and *Donald E. Ward* for GTE Corp., and *Bernard C. Topper, Jr.* and *Mitchell F. Brecher*, for GTE Sprint Communications Corp., were on the joint brief for GTE Corp., *et al.*, intervenors in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, 83-1493, 83-1954, 83-1984, 83-1995, 83-2016, 83-2035, 83-2108, 83-2168, and 83-2218. *Richard McKenna*, *James R. Hobson*, *Gail L. Palivy*, and *Mark P. Bresnahan* also entered appearances for GTE Corp., *et al.*

Charles A. Zielinski and *A. Richard Metzger, Jr.* were on the brief for Rochester Telephone Corp., intervenor in Nos. 83-1225, 83-1463, 83-1464, and 83-1493. *Daniel L. Koffsky* also entered an appearance for Rochester Telephone Corp.

David E. Blabey, *Lawrence G. Malone*, and *Timothy P. Sheehan* were on the brief for New York State Department of Public Service, intervenor in Nos. 83-1225 and 83-1329.

Ronald D. Eastman, *Lynda S. Mounts*, *Louis J. Caruso*, and *R. Philip Brown* were on the brief for the State of Michigan, *et al.*, intervenors in No. 83-1329.

Gary C. Tucker, *Michael L. Glaser*, and *Francis E. Fletcher* were on the brief for Roseville Telephone Company, *et al.*, intervenors in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, and 83-1493.

Leo I. George and *Thomas J. McCabe* were on the statement in lieu of brief for U.S. Telephone, Inc., intervenor in No. 83-1225. *Daniel Huber* also entered an appearance for U.S. Telephone, Inc.

Peter Tannenwald and *Sonya B. McCann* were on the brief for Satelco Inc., *et al.*, intervenors in Nos. 83-1225 and 83-2218. *Mania K. Baghdadi* also entered an appearance for Satelco Inc., *et al.*

Thomas J. O'Reilly was on the brief for United States Independent Telephone Association, intervenor in No. 83-1225.

Edward J. Perez was on the brief for City of Los Angeles, *amicus curiae* urging reversal and remand.

Diane L. McIntire entered an appearance for Iowa State Commerce Commission, intervenor in No. 83-1225.

Eric A. Eisen and *Elisabeth H. Ross* were on the brief for Missouri Public Service Commission, intervenor in No. 83-1329.

Douglas N. Owens also entered an appearance for Washington Utilities & Transportation Commission, intervenor in No. 83-1225.

Theodore D. Frank entered an appearance for Centel Corp., intervenor in Nos. 83-1225, 83-1463, 83-1464, 83-1995, 83-2168, and 83-2218.

Carolyn C. Hill entered an appearance for United Telephone Systems, Inc., intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, and 83-1493.

James H. DeGraffenreidt entered an appearance for Maryland Office of People's Counsel, intervenor in No. 83-1225.

Joseph M. Kittner and *Randolph J. May* also entered appearances for American Broadcasting Companies, Inc., intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, 83-1493, 83-2168, and 83-2218.

Steven M. Schur and *Philip J. Mause* entered appearances for Public Service Commission of Wisconsin, intervenor in No. 83-1225.

Thomas N. Wies entered an appearance for Vermont Public Service Board, intervenor in Nos. 83-1225 and 83-1464.

Elizabeth A. Celis entered an appearance for Arizona Corporation Commission, intervenor in No. 83-1225.

James E. Weging entered an appearance for Illinois Commerce Commission, intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, and 83-1464.

Randall B. Lowe entered an appearance for Combined Network, Inc., intervenor in No. 83-1225.

Nicholas P. Miller entered an appearance for State of Alaska, *et al.*, intervenor in Nos. 83-1225, 83-1329, 83-1439, 83-1463, 83-1464, and 83-1493.

Robert M. Hill, Jr. entered an appearance for Public Service Commission of Alabama, intervenor in No. 83-1225.

William B. Gundling entered an appearance for Department of Public Utility Control of the State of Connecticut, intervenor in Nos. 83-1225 and 83-1984.

Walter Washington entered an appearance for South Dakota Public Utilities Commission, intervenor in Nos. 83-1225 and 83-1329.

David A. Irwin entered an appearance for Enhanced Communication Services Association, intervenor in No. 83-1225.

Stephen R. Bill and *Paul J. Sinderbrand* entered appearances for Tymnet, Inc, intervenor in No. 83-1329.

Gerald R. Tarrant entered an appearance for Public Service of the State of Vermont, intervenor in No. 83-1464.

Randall B. Lowe and *Thomas J. Beers* also entered appearances for Allnet Communication Services, Inc., intervenor in Nos. 83-2035, 83-2168, and 83-2218.

Albert H. Kramer also entered an appearance for American Telephone Association, intervenor in No. 83-2108.

Before: WILKEY and GINSBURG, *Circuit Judges*, and MACKINNON, *Senior Circuit Judge*

Opinion *Per Curiam.*

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PER CURIAM: We review in this proceeding Federal Communications Commission (FCC or Commission) decisions focused on the future of United States interstate telephone services. In the Commission's view, this case presents perhaps "the most difficult" and probably "the most important" problem ever to come before the agency. *MTS & WATS Market Structure: Third Report and Order* ¶ 368, 93 F.C.C.2d 241, 340-41 (1983). The decisions at issue, we conclude, are within the Commission's authority and, for the most part, are rationally grounded and sufficiently supported by evidence. We therefore affirm the FCC's orders in all major respects. We remand to the agency for further, more careful, analysis only two portions of its orders: the segments dealing with party line service and small telephone companies' election of "average schedule company" status.

I. BACKGROUND

A. *AT&T and the Separations Process*

The multiple petitions consolidated for our review address facets of a controversial, compound question: Among telephone users, how should the costs of local telephone company equipment be divided. That equipment starts at every subscriber's wall plug; it includes the line, or "loop," between each subscriber's premises and the local telephone company central office. Switching equipment at the office routes each incoming call out onto the local loop of the subscriber receiving the call, or out to another local office where the call may be switched onto the long-distance lines of AT&T or another long-distance carrier.

A large part of the cost of this local plant is nontraffic sensitive (NTS). Plant costs are nontraffic sensitive when they do not vary with the extent to which the facilities are used. The basic cost of installing and maintaining a local loop, for example, remains the same whether the subscriber, or "end user," uses the loop to

make one call or a hundred, and whether those calls are local or long-distance. Some switching costs, on the other hand, are traffic-sensitive. They in fact increase with usage; for example, as more calls pass through the equipment, heavier, more costly switches must be employed.

In the days when AT&T was the only interstate long-distance carrier, the recovery of telephone equipment costs was not the controversial matter it is today. At first, local telephone companies[1] recovered *all* local exchange plant costs, for the most part through flat per-month charges paid by local subscribers.[2] The long-distance carrier (AT&T for interstate calls, perhaps another company for intrastate long-distance calls) recovered the costs of long-distance or "toll" lines and long-distance switching equipment through usage-sensitive charges imposed on the makers of long-distance calls—the more and farther one called, the more one paid. Where the local carrier owned long-distance property—for example, toll lines out to the city limits—the long-distance carrier reimbursed the local company for the use of that property through a share of long-distance revenues.[3] *See, e.g., Illinois Bell Telephone Co. v. Moyni-*

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[1] Until recently, 22 larger local telephone companies—the Bell Operating Companies (BOCs)—were subsidiaries of AT&T. In 1982, the Justice Department and AT&T entered into a consent decree providing that AT&T would divest itself of the BOCs as of early 1984. *See* United States v. AT&T, 552 F.Supp. 131 (D.D.C. 1982), *aff'd mem.*, 103 S. Ct. 1240 (1983). In addition to the BOCs, almost 1500 independent local companies provide local service.

[2] In the early days of telephone service, pay telephone (coin box) revenues, in addition, were vitally important to local telephone companies. *Cf.* Illinois Bell Tel. Co. v. Moynihan, 38 F.2d 77 (N.D. Ill.) (striking down coinbox rates prescribed by Illinois Commerce Commission as confiscatory), *rev'd*, Smith v. Illinois Bell Tel. Co., 282 U.S. 133 (1930).

[3] When the local company was a subsidiary of AT&T, the reimbursement took place through a division of revenues within the AT&T corporate family.

han, 38 F.2d 77, 82-83 (N.D. Ill.), *rev'd sub nom. Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133 (1930); *Re Indiana Bell Telephone Co.*, 1922C Pub. Util. Rep. 348, 368.

All long-distance calls, however, require the use of both local property and long-distance facilities. The calls begin on some subscriber's local loop; they then travel through local switches on their way out to long-distance lines; from the long-distance lines, they drop back into a local system at the receiving end and pass through local switches; finally, they pass onto the call recipient's local loop. In *Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133 (1930), the Supreme Court decided that, because local plant is used for interstate calls, an appropriate percentage of local plant costs should be placed within the jurisdiction of federal[4] rather than state regulators. AT&T and the local companies then adjusted their cost-allocation system to accommodate *Smith*.

State regulators, after *Smith*, could authorize local companies to recover only the portion of local telephone plant costs allocated to the intrastate jurisdiction. AT&T recovered local telephone plant costs allocated to the interstate jurisdiction and passed those revenues back to the local companies.[5] AT&T chose to recover local telephone costs assigned to the interstate jurisdiction in the same way it had all along recovered costs associated with interstate service—through usage-based charges imposed on the makers of long-distance calls. Thus long-distance callers, charged on the basis of the frequency and dis-

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[4] Prior to the creation of the FCC, *see* Communications Act of 1934, 47 U.S.C. §§ 151-609 (1976 & Supp. V 1981), the Interstate Commerce Commission exercised regulatory authority over interstate wire communication.

[5] All interstate revenues were paid into an interstate "pool." AT&T allocated a share of revenues out of the pool to each local telephone company in proportion to its share of the total

tance of their calls, covered through their payments a significant portion of the costs of local subscriber plant. Revenues paid in by long-distance callers were shared by AT&T with the local companies through a process called settlements and division of revenues.

That basic system remains in effect today. The FCC, working with a Federal-State Joint Board established pursuant to 47 U.S.C. § 410(c) (1976), allocates local plant costs between the interstate jurisdiction (FCC controls recovery of costs) and the intrastate jurisdiction (state commissions control recovery of costs). This mode of allocation—the "separations process"—currently assigns roughly 26% of the costs of local exchange plant to the interstate jurisdiction. *See Amendment of Part 67*, 89 F.C.C.2d 1, 5, *modified*, 90 F.C.C.2d 522, *recon. denied*, 91 F.C.C.2d 558 (1982), *petition for review pending sub. nom. MCI Telecommunications Corp. v. FCC*, No. 82-1237 (D.C. Cir. filed Mar. 4, 1982); *see also MCI Telecommunciations Corp. v. FCC*, 712 F.2d 517, 523 & n.4 (D.C. Cir. 1983).

Two key characteristics of the system bear emphasis. First, local charges do not cover the full costs of local telephone facilities. Today, local charges cover only 74% of the costs of the basic local network. The rest of the local plant costs are recovered from long-distance fees paid by long-distance callers on a traffic-sensitive basis. Second, subscribers who are heavy long-distance users, under the current, usage-based charges, pay a percentage of the costs of the local network wholly out of proportion to the costs of supplying them with service. These subscribers are heavy users of their local loops, but the basic cost of a local loop is nontraffic sensitive—that cost remains the same regardless of how many, or how few, calls a subscriber makes.

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investment allocated to the interstate jurisdiction. *See* Brief for FCC at 10.

B. *The Growth of Alternatives to Ordinary Long-Distance Service*

Ordinary long-distance service is not the only way to arrange calls from one state to another. AT&T and other carriers offer a variety of "private line" arrangements. Private line services furnish to the large-scale user, for a flat rate, full-time private interstate circuits between specific points. Foreign Exchange (FX), for example, is one form of specialized private line service. Essentially, FX users have a private line connected to the local exchange at one end. A Washington business buying Washington-New York FX service with the "closed end" in Washington, under the current scheme, can call any telephone subscriber in New York, without paying an additional per-call charge, and any New York telephone subscriber can call the business in Washington for the price of a local call. Common Control Switching Arrangement (CCSA) is another specialized private line service. CCSA involves a network of private lines linked through switches at a local telephone company's premises. *See Bell System Tariff Offerings*, 46 F.C.C.2d 413, 418 n.5, *aff'd sub nom. Bell Telephone Co. v. FCC*, 503 F.2d 1250 (3d Cir. 1974), *cert. denied*, 422 U.S. 1026 (1975).

The FCC, prior to the set of decisions before us for review, did not require users of private line services to contribute, as ordinary long-distance callers do, to local plant costs allocated to the interstate jurisdiction. Users of these services, however, may in fact place long-distance calls originating and/or terminating in the local exchange. For example, every FX call is an interexchange call originating or terminating in a local exchange. FX users now pay ordinary business line rates (as well as a flat fee for the private line) and thus contribute to local plant costs allocated to the *intrastate* jurisdiction; currently, however, they make no contribution to the local plant costs allocated to the interstate jurisdiction. A further illustration is the "leaky PBX." The "leaking"

becomes possible when a private line user hooks up its private line to an ordinary local loop through a switchboard, or "PBX," at one or both ends. A business with a New York-Washington private line can thus dial up from any Washington exchange telephone to the Washington switchboard, dispatch the call to New York via the private line, and drop it back out into the New York local exchange through the switchboard on the other end. Here too, the caller currently makes no contribution to local plant costs allocated to the interstate jurisdiction.

Choice increased when other common carriers (OCCs) entered the market once served only by AT&T. The Commission's decision in *Specialized Common Carrier Services*, 29 F.C.C.2d 870 (1971), *aff'd sub nom. Washington Utilities & Transportation Commission v. FCC*, 513 F.2d 1142 (9th Cir.), *cert. denied*, 423 U.S. 836 (1975), paved the way for private line market entry by carriers offering services in competition with AT&T. Subsequent FCC and appellate court decisions clarified that AT&T could not, through its subsidaries, the Bell Operating Companies (BOCs), block competition in private line offerings, such as FX and CCSA, by denying OCCs loop service through which they could interconnect their private line circuits into the local exchange. *See Bell System Tariff Offerings*, 46 F.C.C.2d 413, *aff'd sub nom. Bell Telephone Co. v. FCC*, 503 F.2d 1250 (3d Cir. 1974), *cert. denied*, 422 U.S. 1026 (1975).

In 1974 MCI filed tariffs for a new service it called Execunet. With Execunet, MCI linked together a nationwide network of intercity private lines and local interconnections to offer a service that could compete with AT&T's ordinary long-distance service. An Execunet customer could enter the MCI network from any local phone in an area served by the network and, after entering a subscriber authorization code, dial an ordinary long-distance number. The call would travel over MCI

private facilities to the appropriate local exchange, drop back into the local exchange, and be routed along local lines to its recipient. This court, in its *Execunet I* and *II* decisions, held that Execunet service was not beyond the scope of MCI's private line authorizations; that the Commission had not made the explicit public interest findings necessary to bar OCCs from offering such service; and that, unless and until the Commission made such findings, local telephone companies were required to give the OCCs appropriate interconnections for the service. *MCI Telecommunications Corp. v. FCC*, 561 F.2d 365 (D.C. Cir. 1977), *cert. denied*, 434 U.S. 1040 (1978) (*Execunet I*); *MCI Telecommunications Corp. v. FCC*, 580 F.2d 590 (D.C. Cir.), *cert. denied*, 439 U.S. 980 (1978) (*Execunet II*).

After the *Execunet* decisions, the FCC opened Common Carrier Docket No. 78-72 to determine "whether the public interest requires that interstate message toll telephone service (MTS) [*i.e.*, ordinary long-distance service] and/or wide area toll telephone service (WATS), or their functional equivalents, should be provided . . . free from direct competition[]." *MTS & WATS Market Structure: Notice of Inquiry and Proposed Rulemaking*, 67 F.C.C.2d 757, 757 (1978) (footnotes omitted). The Commission announced that it would consider, as part of its analysis,

> what reimbursement interstate services should make to local operating companies for the use of local plant, on a cost causational basis; what additional charges, if any, should be levied on interstate services to support local exchange services; and whether and how these charges can be equitably imposed on all interstate services.

Id. at 759.

During the pendency of the *Execunet* litigation, the OCCs and their subscribers made no contribution to local plant costs allocated to the interstate jurisdiction. In

1978, however, the BOCs filed a new tariff with the FCC under which OCCs would pay for Exchange Network Facilities for Interstate Access (ENFIA) at rates designed to parallel the contribution AT&T made to the costs of local plant through the settlements and division of revenues process. The OCCs, the BOCs claimed, were using local exchange plant to make interstate calls in the same manner as AT&T—yet the OCCs made no special contribution to the costs of that plant, as AT&T did. The ENFIA tariff was the remedy the BOCs proffered for this disparity.

The OCCs protested vigorously. Their interconnections into the local exchange, they argued, were simple FX interconnections to the "line side" of a local central office switch. FX users had never contributed to the interstate portion of local plant costs. AT&T's interconnection to the "trunk side" of a toll office switch, the OCCs pointed out, was different and, at the time of the ENFIA tariff filing, technologically available only to AT&T. "Trunk side" connection, the OCCs maintained, was far superior to "line side" linkage. Because of the unique quality of AT&T's interconnection, the OCCs argued, AT&T was the only true provider of ordinary long-distance services. Thus, in the OCCs' view, AT&T should shoulder alone the costs of local exchange plant allocated to the interstate jurisdiction.

To cope with this dispute pending eventual action in Docket No. 78-72, the FCC in 1978 supervised several months of negotiations. The Commission's objective was to achieve "some form of a 'rough justice' interim" solution. *AT&T*, 91 F.C.C.2d 1079, 1081 (1982). The negotiations culminated in December 1978 with the signing of the ENFIA agreement, a settlement due to expire, by its terms, upon the effective date of a superseding Commission order in Docket No. 78-72, or after five years, whichever came first. Under the ENFIA agreement OCCs providing Execunet-type services made "pay-

ment[s] to the local telephone company for use of jointly used subscriber plant . . . in the provision of their interstate services." ENFIA Agreement ¶ 9, *reprinted in* 43 Fed. Reg. 59,129, 59,131 (1978). These payments, however, were far below those AT&T made through the settlements and division of revenues process.

Parties to the ENFIA agreement remained mindful of the disparate treatment of Execunet-type services in comparison to other interstate services, whose providers paid only local business rates for connections to local exchange facilities. They were mindful also that an attempt to arrive at a more encompassing settlement might have impeded negotiations. *See MCI Telecommunications Corp. v. FCC*, 712 F.2d 517, 524 (D.C. Cir. 1983). The ENFIA settlement therefore stated that the parties reached their interim agreement on compensation of local telephone companies for use of local exchange facilities "as if" the charges they established "could, after appropriate consideration by the Commission, be ultimately applied to other services which also utilize the local telephone company exchange facilities." ENFIA Agreement ¶ 5, *reprinted in* 43 Fed. Reg. at 59,131.

C. *Proceedings in Docket No. 78-72*

The Commission did not linger over the basic market structure issue in Docket No. 78-72; it concluded that an open market and free competition were "in the public interest and will further the goals of the Communications Act." *MTS & WATS Market Structure: Report and Third Supplemental Notice of Inquiry*, 81 F.C.C.2d 177, 183 (1980) (*Third Supplemental Notice*). Turning to the further issues posed in the docket, the Commission, after four supplemental notices of inquiry, ultimately released *MTS & WATS Market Structure: Third Report & Order*, 93 F.C.C.2d 241 (1983) (*Access Order*), the first of the series of FCC orders presented for our review. The Commission twice modified the *Access Order*

plan, initially and most substantially on reconsideration, *MTS & WATS Market Structure: Memorandum Opinion & Order*, 48 Fed. Reg. 42,984 (1983) (*Reconsideration Order*), and again on further reconsideration, *MTS & WATS. Market Structure: Memorandum Opinion & Order*, 49 Fed. Reg. 7,810 (1984) (*Further Reconsideration Order*). All three orders are before us in this appellate proceeding.

In its Docket No. 78-72 dispositions, the Commission sought to accommodate four goals that tugged in different directions. "[T]he continued assurance of universal service" appeared first on the FCC's list. *Access Order* ¶ 122, 93 F.C.C.2d at 278. Section 1 of the Communications Act requires the FCC to "regulat[e] interstate . . . commerce in communication by wire and radio so as to make available, so far as possible, to all people of the United States a rapid, efficient, Nationwide and worldwide wire and radio communication service with adequate facilities at reasonable charges." 47 U.S.C. § 151. Our case law recognizes the prominence of this universal service objective. *See, e.g., United States v. Western Electric Co.*, 569 F.Supp. 1057, 1120 (D.D.C. 1983); *see also Access Order* ¶¶ 74-84, 93 F.C.C.2d at 265-67.[6] The other three objectives identified by the Commission were "the elimination of unjust discrimination or unlawful preferential rates," as mandated by section 202 of the Communications Act; "the encouragement of network efficiency"; and "the prevention of uneconomic bypass." *Access Order* ¶ 122, 93 F.C.C.2d at 278.

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[6] MCI contends that the FCC has no responsibility to promote universal service because "the Commission has no statutory responsibility for local communications," and therefore "it would be unlawful for it to promulgate a policy designed to . . . benefit local communications." Brief for Intervenor MCI Telecommunications Corp. at 19 n.20. We reject MCI's argument. Congress directed that, "so far as possible, . . . *all* people of the United States" are to have adequate telephone facilities at reasonable prices.

"Bypass" occurs when end users develop and employ alternative local distribution technologies in place of the local exchange system. The Commission considered certain forms of bypass a grave risk. It feared, particularly, that the current system for recovery of subscriber plant costs might lead to "uneconomic bypass"—that heavy users might turn to bypass technologies priced lower than local exchange facilities, but in fact costing more to provide. The Commission explained that "uneconomic" technologies posed a threat to the local telephone network when, as under the current system of charges, access to the local telephone network, for heavy interstate users, is priced above cost. This ultimate concern influenced the FCC's course: if large users left the network and turned to bypass technologies, the local companies would have to raise the rates paid by their remaining subscribers, thus jeopardizing universal service.

The Commission determined that its various objectives could be balanced most effectively if it moved toward a system in which a substantial portion of the NTS costs of local telephone plant within the FCC's jurisdiction would be recovered through flat per line charges billed to end users. The FCC targeted for elimination heavy long-distance users' payment of a share of local telephone plant costs in excess of the actual cost of supplying those users with service. A critical factor, sometimes overlooked in discussions of the cost-allocation problem the FCC faced, was spotlighted by the Commission: "A subscriber who does not use the subscriber line to place or receive calls imposes the same NTS costs as a subscriber who does use the line." *Access Order* ¶ 121, 93 F.C.C.2d at 278. It should be the main rule, the FCC decided, that subscribers bear responsibility for the local telephone network costs they actually cause. Explaining its position, the Commission stated:

> Economics teaches us that, except in certain circumstances involving market failure, prices equal to

the cost of producing another increment of a good, i.e., equal to the marginal cost of production, are optimal. Provision of telephone services involves two marginal costs. One varies with the traffic level. The other varies with the number of access lines demanded. For this reason, efficient pricing requires both usage sensitive and non-usage sensitive charges for recovery of access costs.

The cost imposed upon the nation's telecommunications system, and ultimately upon the general public, by our present usage sensitive method of recovering these NTS costs pose[s] a substantial danger to the long term viability of our nation's telephone systems. New technologies and radical improvements in older technologies make available alternatives to the traditional telephone network. Telecommunications is substitutable for a wide variety of other goods and services produced by our society. Prices based upon the true cost characteristics of telephone company plant are necessary both to make a decision on whether use of the alternative technologies is appropriate and to make a decision on whether to substitute telecommunications for other activities.

As telecommunications plays a larger and larger role in fundamental U.S. industries, the problems resulting from inappropriate pricing grow. Computer technology and communications have grown so similar that the Commission has redrawn its traditional definition of communications. Access pricing that does not reflect cost can turn computer technologies from directions that would enhance the productivity of this essential U.S. industry and all of the industries that depend on computers and communications toward simple avoidance of non-cost based telecommunications prices. Investment may be misdirected as a result.

Id. ¶¶ 27-29, 93 F.C.C.2d at 251-52 (footnotes and paragraph numbers omitted).

The FCC acknowledged that "uncertainty surround[ed] the precise size and threat of uneconomic bypass," but found the bypass phenomenon real and growing. *Id.* ¶ 31, 93 F.C.C.2d at 252. It would be unwise, the Commission concluded, to delay implementation of a cost-based pricing system until the effects of bypass became more pronounced. Delay risked losing "the luxury of the gradual transition needed to satisfy our objective of maintaining affordable service"; any further bypass "might mean higher long run costs for those who were required to remain on the network." *Id.* Of prime importance in its decisionmaking, the Commission observed:

> [W]ere we to delay instituting the smooth movement towards a rational pricing system until a significant number of large users had initiated constructing alternative bypass systems, it could well be too late for any remedial action. Usually uneconomic bypass is uneconomic only before the construction of bypass facilities starts. Once a large telecommunications user has committed significant capital to building a private bypass system, the maintenance of that system is no longer uneconomic. Consequently, we believe that prompt action is essential to preserve the public interest.

Id. ¶ 32, 93 F.C.C.2d at 252-53.

Under the FCC's plan to shift most subscriber plant costs in the interstate jurisdiction onto end users, a $6 end user charge will be imposed on multi-line business customers starting in June 1984. The Commission now anticipates imposing some end user charges on residential and single-line business users, on a transitional basis, starting in June 1985. The initial *Access Order* contemplated recovery through flat-rate end user access charges of all NTS subscriber plant costs except those allocated to a carrier-supported Universal Service Fund, designed to keep down local rates in areas where exchange plant costs are especially high. *Access Order*

¶ 134, 93 F.C.C.2d at 281-82. On reconsideration, the Commission chose to institute further decisionmaking on several matters: the magnitude of the end user charge after the transition; categories of low-income subscribers who should be exempted from end user charges; the shape of the transition; and mechanisms sensitive to the particular needs of small telephone companies in high cost areas. The residential and single-line business end user charge will not exceed $4 per line per month through 1990, and the FCC has announced its intention to monitor closely the impact of residential end user charges on universal service as those charges are imposed. *Further Reconsideration Order* ¶¶ 15-26, 49 Fed. Reg. 7,810, 7,812-13 (1984).

The FCC has allocated the jurisdictionally interstate NTS costs of local telephone plant that it is not shifting to end users—or, for the transitional period, that it is not yet shifting to end users—to interexchange carriers and to users of interstate private line services. Interexchange carriers are to pay a "carrier's carrier" charge; a surcharge has been established for private line users. The interexchange carriers (most prominently, AT&T and the OCCs) will in turn pass their carrier's carrier charge on to their customers through the long-distance rates they set. The modified final judgment settling the government's antitrust suit against AT&T, *see supra* note 1, requires the BOCs to move, over the next few years, to provision of equal interconnection to the OCCs; to the extent that the same quality interconnection is unavailable in the transitional years, AT&T's carrier's carrier charge will be maintained at a "premium" above the charge paid by the OCCs. The interim surcharge set by the Commission is to be paid by the following category of users: private line and other users who may engage local exchanges for interstate calling without otherwise contributing to the portion of local telephone plant costs assigned to the interstate jurisdiction.

D. *Review of the FCC's Orders*

Our review of the FCC's multifaceted decision first considers arguments relating to the Commission's imposition of flat-rate end user access charges. Under this main heading, we deal with (1) contentions that the imposition of end user charges exceeds jurisdictional limitations on the Commission's authority implicit in the Communications Act and/or the Supreme Court's decision in *Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133 (1930); [7] (2) assertions that the FCC's decision is irrational, unsupported, or procedurally defective; [8] and (3) attacks on the end user charges the Commission ordered for Centrex-CO subscribers [9] and party-line users.[10] We also place in this portion of the opinion review of the Commission's changes in the prerequisites for small tele-

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[7] This position is advanced by petitioners National Association of Regulatory Utility Commissioners and California, and by intervenors National Association of State Utility Consumer Advocates, *et al.*, Florida Public Service Commission, New York State Department of Public Service, Independent Alliance, and Missouri Public Service Commission. It is addressed by the FCC and intervenors MCI Telecommunications Corp., AT&T, BOCs, United States Independent Telephone Association, IBM Corp., and Rochester Telephone Company.

[8] These arguments are made by petitioners National Associaction of Regulatory Utilities Commissoners and California, and by intervenors National Association of State Utility Consumer Advocates, Michigan, Rural Telephone Coalition, Florida Public Service Commission, and Independent Alliance. They are addressed by the FCC and intervenors AT&T, BOCs, United States Independent Telephone Association, and Rochester Telephone Company.

[9] Parties mounting these attacks are petitioners Public Service Commission of the District of Columbia and North American Telecommunications Association. The FCC, supported by intervenors BOCs and ROLM Corp., defends its actions.

[10] This attack is made by petitioner Rural Telephone Coalition.

phone companies' election of "average schedule company" status.[11]

In the second main segment of the opinion, we address objections various petitioners raise to the carrier's carrier charge and private line surcharge. These objections include claims that (1) the FCC's plan perpetuates unlawful discrimination between OCCs and other entities using the local exchange for interstate calling;[12] (2) the FCC's prescription of a surcharge payable by private line and other users lacks evidentiary support or rational basis;[13] (3) the FCC's action regarding private communications systems is unjustified;[14] and (4) errors warranting reversal infect the FCC's treatment of FX users.[15]

II. ANALYSIS

A. *Flat-Rate End User Access Charges*

1. *FCC Authority to Impose the Charges*

Petitioners[16] present, elaborate, and recapitulate their core argument that the Commission lacks authority to impose flat-rate end user access charges. They derive

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[11] *See supra* note 10.

[12] Petitioner MCI Telecommunications Corp. and intervenor Satelco, *et al.* make this claim; the FCC's position is supported by intervenors AT&T, BOCs, GTE Corp., Ad Hoc Telecommunications Users Committee, and Association of Data Processing Service Organizations.

[13] Petitioner Aeronautical Radio, Inc. and intervenor American Petroleum Institute, *et al.* make this claim; the FCC is supported by intervenors AT&T and BOCs.

[14] Intervenor American Petroleum Institute levels this attack.

[15] Petitioner Aeronautical Radio, Inc. here contests the FCC's decision; intervenors AT&T and BOCs defend the FCC.

The validity of the premium carrier's charge levied against AT&T above that assessed against the OCCs is under consideration in a separate review proceeding. AT&T v. FCC, No. 84-1087 (D.C. Cir. filed March 9, 1984).

[16] "Petitioners," as used in our analysis, describes both petitioners and intervenors appearing in opposition to the Commission's decision.

their contentions from precedent and statutory provisions. We turn first to their insistent claim that the Supreme Court's decision in *Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133 (1930), *see supra* p. 21, confirms the powerlessness of the federal agency to take the action they challenge. Petitioners misapprehend the Court's holding in *Smith*. We here describe that case in sufficient detail to clarify the precise thrust of the High Court's opinion.

Smith presented for Supreme Court review a district court decision striking down as confiscatory Chicago coin-box rates set by the Illinois Commerce Commission. The district court, like the state commission before it, had taken as a rate base all of Illinois Bell's Chicago property, including both exchange plant and toll (long-distance) lines out to the city limits. In computing the revenue generated by that investment, the district court counted both the sums Illinois Bell received directly from local users and the share of interstate tolls AT&T paid over for the use of Illinois Bell's long-distance lines in interstate calling.

The Supreme Court reversed. It held first that the state commission and district court erred in not separating out Illinois Bell's intrastate and interstate property, revenue, and expenses. Chief Justice Hughes wrote:

> The separation of the intrastate and interstate property, revenue and expenses of the Company is important not simply as a theoretical allocation to two branches of the business. *It is essential to the appropriate recognition of the competent governmental authority in each field of regulation.* In disregarding the distinction between the interstate and intrastate business of the Company, the court found it necessary to pass upon the fairness of the division of interstate tolls between the American and Illinois companies. The court held that the division was reasonable and the appellants contest this ruling. But

> the interstate tolls are the rates applicable to interstate commerce, and neither these interstate rates nor the division of the revenue arising from interstate rates was a matter for the determination either of the Illinois Commission or of the court in dealing with the order of that Commission.

282 U.S. at 148 (emphasis supplied). The Court stated that it was the ICC, then charged with regulating interstate communication, *see supra* note 4, that had "authority to estimate the value of the property used in the interstate service and to determine the amount of the revenues and the expenses properly attributable thereto"; "[t]he proper regulation of rates can be had only by maintaining the limits of state and federal jurisdiction." *Id.* at 149. Any review of the state commission's order, the Court continued, must therefore rest on an appropriate determination of "the value of the property employed in the intrastate business and of the compensation receivable for the intrastate service." *Id.* The Court cited the *Minnesota Rate Cases*, 230 U.S. 352, 435 (1913), in which it had imposed a similar constraint on the states' determination of intrastate rail rates.[17]

The requisite allocation of property between the interstate and intrastate services, the Court then stated, must be made with an eye to "the actual uses to which the property is put." 282 U.S. at 151. Figures Illinois Bell had submitted to the district court reflected treatment of the costs of exchange plant as wholly local. *Id.* at 150. That allocation was impermissible, the Court declared, "for unless an apportionment is made, the intrastate service to which the exchange property is allocated will bear an undue burden." *Id.* at 151.[18]

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[17] In a later opinion, Chief Justice Hughes characterized *Smith* as "a case where the segregation of properties and business was essential in order to confine the exercise of state power to its own proper province." Lone Star Gas Co. v. Texas, 304 U.S. 224, 241 (1938).

[18] Petitioners emphasize this statement. *See, e.g.*, Brief of Petitioner National Association of Regulatory Utility Com-

One petitioner argues that *Smith* precludes FCC-imposed flat-rate end user charges because the imposition means "costs attributable to interstate usage [are not] allocated to and recovered from the interstate network." Brief of Petitioner National Association of Regulatory Utility Commissioners at 28 (hereafter, NARUC Brief). Another asserts that the FCC's plan "essentially repeals" *Smith*'s command to allocate exchange plant between the interstate and intrastate jurisdictions. Brief of Intervenor National Association of State Utility Consumer Advocates, *et al.* at 13 (hereafter, NASUCA Brief). *See also* Brief of the People of the State of California and the Public Utilities Commission of the State of California at 11 (hereafter, California Brief); Brief of Intervenor Florida Public Service Commission at 16 (hereafter, Florida Brief).

Petitioners confuse or blend two questions: (1) jurisdiction or authority to recover costs; (2) the manner in which costs are to be recovered. *Smith* dealt with jurisdiction; it held that a portion of the costs of local subscriber plant may be recovered only under the authority of a body with interstate regulatory powers. The *Smith* Court did not address the manner in which the federal agency was to perform its task. It did not hold that the FCC must order recovery of costs allocated to its juris-

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missioners at 26; Brief of Intervenor National Association of State Utility Consumer Advocates, *et al.* at 14 (hereafter, NASUCA Brief); Brief of Intervenor New York State Department of Public Service at 21. They argue that the FCC's plan is inconsistent with *Smith* because under the FCC's plan "local exchange customers . . . bear all the burden." NASUCA Brief at 20.

We read less into the Court's words. The state commission, the Court explained, must count some exchange plant as interstate to avoid retaining interstate property, but not interstate revenues, in its calculations. By including interstate property in its jurisdictional domain, the state commission would artificially inflate the intrastate rate base, and hence intrastate charges.

diction through usage-based charges. The practical effect of the *Smith* decision in 1930, it is true, was a system under which subscriber plant costs in the interstate jurisdiction would be recovered on a usage basis. But nothing in *Smith* mandated that result; other plans under which those costs were subject to federal, rather than local, regulatory authority might have served as well.[19]

[19] Some petitioners argue that their view of *Smith* became statutory law when Congress enacted 47 U.S.C. § 410(c) (1976). *See* NASUCA Brief at 16-23. Section 410(c) provides for the establishment of a Federal-State Joint Board to make recommendations to the FCC with regard to the separations process. The provision was introduced in 1971 at the urging of the National Association of Regulatory Utilities Commissioners (NARUC). NARUC complained that the FCC was allocating too many costs to the intrastate jurisdiction, to be recovered through local charges, and not enough to the interstate jurisdiction, to be recovered through AT&T long distance charges. *See* 117 CONG. REC. 15,979-81 (1971).

NASUCA contends that the FCC's plan "reduces the Joint Board proceedings under § 410(c) to a mere sham." NASUCA Brief at 19. We cannot agree; Joint Board proceedings, now as before, determine which costs shall be allocated to the jurisdiction of the state commissions and which to the jurisdiction of the FCC. As support for the position that *Smith* and the § 410(c)-endorsed separations process go beyond jurisdiction and indeed dictate how costs must be recovered, NASUCA cites material printed in the Congressional Record by Senator Magnuson when he introduced the Senate version of § 410(c). The material states that the separations process should avoid placing any "unreasonable burden . . . on either the interstate or intrastate users of the telephone service." It emphasizes the importance of local service, and of "allocat[ing] a fair amount of the cost of providing local telephone service to the users of the interstate service." 117 CONG. REC. 15,980 (1971). NASUCA leans too heavily on these words. When § 410(c) was enacted, local telephone plant costs in the interstate jurisdiction were in fact recovered through usage-based charges. Senator Magnuson may have been concerned with protecting the legitimate interests of the state commissions under that system. Nothing in the legislative history of § 410(c), however, convinces us that the section was meant to freeze in place for all time the 1971 system for recovery of costs.

Coupled with their exorbitant reading of *Smith v. Illinois Bell Telephone Co.*, petitioners assert that section 2(b) of the Communications Act,[20] which denies Commission jurisdiction over purely intrastate communications, precludes the FCC's imposition of flat-rate end user charges.[21] Those charges, petitioners say, are in fact for intrastate, not interstate, service. They must be paid

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[20] Section 2(b) reads in part:

> [S]ubject to the provisions of section 301 of this title, nothing in this chapter shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities or regulations for or in connection with intrastate communication service by wire or radio of any carrier, or (2) any carrier engaged in interstate or foreign communication solely through physical connection with the facilities of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier . . . except that sections 201 to 205 of this title shall, except as otherwise provided therein, apply to carriers described in clause [] (2) . . . .

47 U.S.C. § 152(b) (Supp. V 1981).

[21] Petitioners also cite § 221(b) of the Act, which reads:

> Subject to the provisions of section 301 of this title, nothing in this chapter shall be construed to apply, or to give the Commission jurisdiction, with respect to charges, classifications, practices, services, facilities, or regulations for or in connection with wire, mobile, or point-to-point radio telephone exchange service, or any combination thereof, even though a portion of such exchange service constitutes interstate or foreign communication, in any case where such matters are subject to regulation by a State commission or by local governmental authority.

47 U.S.C. § 221(b) (1976).

Section 221(b) is irrelevant to the problem before us; its limitation on Commission regulation of telephone exchange service "was merely intended to preserve state regulation of local exchanges that happen to overlap state lines." Computer and Communications Indus. Ass'n v. FCC, 693 F.2d 198, 216 (D.C. Cir. 1982), *cert. denied,* 103 S. Ct. 2109 (1983).

to receive *any* telephone service; even subscribers who neither make nor receive interstate calls in the billing period must pay. Thus, petitioners conclude, the charges should be regarded as a "local access" toll, an intrastate rate, a directive the FCC lacks jurisdiction to impose. *See* Brief of Intervenor New York State Department of Public Service at 9-10, 19 (hereafter, New York Brief); California Brief at 11; Florida Brief at 18.

Petitioners here lose sight of the Commission's main theme. The end user charge reflects costs caused not by a subscriber's actually making interstate calls, but by the subscriber's connection into the interstate network, which enables the subscriber to make interstate calls. The same loop that connects a telephone subscriber to the local exchange necessarily connects that subscriber into the interstate network as well. Under *Smith*, a portion of the costs of that loop are assigned to the interstate jurisdiction, for recovery under the regulatory authority of the FCC, on the basis of a complex division taking into account statistical calling patterns. That separations decision, however, does not affect the cost of the loop. Local telephone plant costs are real; they are necessarily incurred for each subscriber by virtue of that subscriber's interconnection into the local network, and they must be recovered regardless of how many or how few interstate calls (or local calls for that matter) a subscriber makes. The FCC may properly order recovery, through charges imposed on telephone subscribers, of the portion of those costs that, in accordance with *Smith*, have been placed in the interstate jurisdiction.

In *North Carolina Utilities Commission v. FCC*, 552 F.2d 1036 (4th Cir.), *cert. denied*, 434 U.S. 874 (1977) (*NCUC II*), the Fourth Circuit reviewed a Commission order setting conditions under which terminal equipment (including home telephones, answering devices, and switchboards) could be connected to local telephone company lines. The order covered, inter alia, subscribers who neither made nor received interstate calls. Petitioners in

NCUC II argued that the Commission had impermissibly invaded the intrastate jurisdiction; the FCC, they objected, had set rules for use of equipment needed, and used dominantly—sometimes exclusively—for local calls. The Fourth Circuit rejected the argument that the FCC had trespassed on state territory. The terminal equipment in question, it noted, was used for both interstate and intrastate communication. "The withdrawal of [FCC] jurisdiction over one," the court stated, "cannot be read to mean the withdrawal as to the other," 552 F.2d at 1046, nor could the fact that the phones were necessary for local calling divest the FCC of its "paramount" interstate regulatory authority. *Id.* at 1043 (describing holding of *North Carolina Utilities Commission v. FCC*, 537 F.2d 787 (4th Cir.), *cert. denied*, 429 U.S. 1027 (1976) (*NCUC I*)). The court concluded:

> Petitioners confuse the fact that almost all terminal equipment is and has been used predominantly for local communication, with the statutory division of decisionmaking power. We find it difficult to credit an argument which amounts to an assertion that Congress created a regulatory scheme that depends on the calling habits of telephone subscribers to determine the jurisdictional competence of the FCC versus state utility commissions.

552 F.2d at 1046.

We endorsed the Fourth Circuit's *NCUC I* and *II* reasoning in *Computer and Communications Industry Association v. FCC*, 693 F.2d 198 (D.C. Cir. 1982), *cert. denied*, 103 S. Ct. 2109 (1983) (*Computer II*). That case presented for review a Commission order detariffing terminal equipment (there described as customer premises equipment, or CPE), including home telephones, and preempting all state rate regulatory authority in the area. Petitioners in *Computer II* asserted that "the Commission's decision to order the states to remove CPE charges from their tariffs is an unjustifiable invasion of the authority to regulate intrastate communications services re-

served to the states by the Act." 693 F.2d at 214. The *NCUC II* court had noted that it did not have before it an FCC attempt "to control the *rates* for exclusively local service." 552 F.2d at 1047 (emphasis in original). We rejected an attempt to distance *NCUC II* from *Computer II* on that ground, and said we saw no reason to distinguish between "preemption principles applicable to state ratemaking authority and those applicable to other state powers." 693 F.2d at 215, 216.

In *Computer II* the FCC asserted exclusive rate regulatory authority over CPE; we upheld its order, although the equipment in question is necessary to make local calls, and although some subscribers might use their CPE only to make local calls. Similarly here, the FCC asserts authority to condition end user access to the local telephone plant on the end user's payment of plant costs in the FCC's interstate domain, although the plant in question is necessary to make local calls, and although some subscriber's might use it only to make local calls. In each case, the very same equipment is by its nature a key element of both interstate and intrastate calling. Every telephone subscriber is automatically connected through the same subscriber plant into both the local exchange and the interstate network. No subscriber can avoid "causing" those costs of its telephone line allocated to the interstate jurisdiction.

Counsel for petitioner NARUC indicated at oral argument that NARUC's jurisdictional objection would evaporate if a mechanism could be utilized to allow end users who elected not to make or receive interstate calls to escape payment of local telephone plant costs allocated to the interstate jurisdiction. Oral Argument Transcript at 28. This argument would make some sense if a subscriber's choice not to make interstate calls meant that certain fixed "interstate" costs would not be incurred; if that were in fact the case, it might well be unfair to ask a subscriber who neither made nor received inter-

state calls to pay those costs. A subscriber's choice not to make or receive interstate calls, however, would not reduce the costs of that subscriber's loop; the local telephone plant costs would remain unchanged, as would the need to recover those costs. If we indulged NARUC's claim—that jurisdictional significance attends an individual subscriber's decision to use its line entirely for intrastate calls—then, as NARUC's counsel conceded, NARUC could hardly contest an allocation of all of such a subscriber's line costs (previously divided between the interstate and intrastate domains) to the intrastate jurisdiction alone. *See id.* at 22-23. It is hard to see what significant benefit NARUC would gain under such an arrangement.[22]

The scheme advanced by the FCC simply requires all telephone subscribers to pay, on a per-line basis, for that portion of *their necessarily-incurred local telephone plant costs* assigned under *Smith* to the interstate jurisdiction. We cannot sensibly say that the FCC has overstepped the limits of its jurisdiction in embarking upon such an arrangement.[23]

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[22] In practice, such an adjustment would be unworkable. It would be prohibitively complex and inefficient to have the separations formula vary from subscriber to subscriber. Any equivalent adjustment would have to be based on the totality of subscriber plant investment and expenses.

[23] California additionally argues that the Commission's power under § 205 of the Communications Act should be limited by § 203, which provides that all communications common carriers except "connecting carriers"—including those engaged in interstate communications "solely through physical connection with the facilities of another [unrelated] carrier," 47 U.S.C. §§ 153(u), 152(b) (1976 & Supp. V 1981)—must file public schedules of their charges for interstate wire or radio communication. California reasons that just as connecting carriers are exempt from the tariff-filing requirement of § 203, they should be immune from Commission power under § 205. California Brief at 12. Sections 203 and 205, however, serve different goals. The § 203 filings of a non-connecting carrier in any case show "all charges for itself and its connecting carriers," 47 U.S.C. § 203, and nothing in § 203 pre-

2. *The FCC's Decisional Process*

Petitioners unleash a volley of argument attacking the FCC's decisionmaking process as unreasoned or unreasonable. They claim that the FCC misjudged the threat of economic bypass, inadequately considered the potential harm to universal service, and failed to observe necessary or proper procedural requirements during the rulemaking.

a. Uneconomic Bypass

Most prominently, petitioners say the evidence before the Commission did not warrant an immediate response of the kind the FCC gave to the prospect of uneconomic bypass. If heavy users of interexchange services can cut costs through bypass technologies, petitioners concede, the risk of bypass is present. But the Commission should have held back, they contend. Technologically, petitioners maintain, bypass potential has not matured as a marketplace force to be reckoned with. "[R]egulation perfectly reasonable and appropriate in the face of a given problem," petitioners remind us, "may be highly capricious if that problem does not exist." NARUC Brief at 39 (quoting *Home Box Office, Inc. v. FCC*, 567 F.2d 9, 36 (D.C. Cir.), *cert. denied*, 434 U.S. 829 (1977)).[24]

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vents the Commission from thus evaluating the charges of connecting carriers, finding them unlawful, and prescribing just and reasonable charges under § 205. Further, California's argument that connecting carriers are wholly safe from the Commission's § 205 power seems hard to reconcile with 47 U.S.C. § 152(b), which provides that "sections 201 to 205 of this title shall, except as otherwise provided therein, apply to [connecting carriers]." *But see* New York Brief at 11-12, 23-24 (quoting § 152(b) but omitting crucial language).

[24] *But cf.* California Brief at 16, 18 ("Today, . . . as a result of the historical development of alternative means of communications, most large users have already bypassed the local exchange"; nonetheless, "the limited threat posed by 'uneconomic' bypass does not justify the extreme measures proposed by the FCC.").

We hold that the FCC's treatment of the bypass issue is adequately reasoned and indicate here why we have so concluded. We turn first to the staff effort preceding the Commission's determination.

During the past few years, members of the communications industry have been bombarded with press and trade writings promoting the use and virtues of bypass technology. Status Report on Near-Term Local Bypass Developments 6 (attached to *Access Order* as Appendix F), *reprinted in* J.A. 3101, 3106 (hereafter, Appendix F). Many of these materials came to the Commission's attention in the commenting process. The Commission staff did not swallow the materials whole. It prepared and submitted to the Commission a preliminary report based on its own survey of the industry and the current literature. *Id.* at 1, *reprinted in* J.A. 3101, 3101. The report documents the reality of both local and long-haul bypass. We cite several examples.

Martin Marietta connects its Data Systems Center to its Orlando plant via fiber optic cable; it is currently installing an earth station to bypass the local exchange and make interstate calls directly via satellite. Southern Bell estimates its current gross revenue loss from Martin Marietta's self-help at an annual $500,000, and its projected annual revenue loss at up to $3 million. *Id.* at A-3, *reprinted in* J.A. 3101, 3128. Southern Railway System uses a private microwave system in three states (Alabama, Georgia, Kentucky); South Central Bell estimates its resulting yearly revenue loss at $300,000. *Id.* Combustion Engineering completely bypasses the local network for long-distance calling; Southern New England Telephone estimates the revenue loss to it at $1.7 million per year. *Id.* at A-4, *reprinted in* J.A. 3101, 3129. Textronics operates a digital microwave system linking various of its facilities in Oregon and Washington; Pacific Northwest Bell estimates its revenue losses at $800,000 per year. *Id.* at A-5, *reprinted in* J.A. 3101, 3130. The federal government utilizes digital satellite

links to connect its Seattle switching network with a California switching node; Pacific Northwest Bell estimates its revenue losses at $1.5 million per year. *Id.* Boeing uses a digital microwave system linking several of its facilities in the Puget Sound basin, causing Pacific Northwest Bell revenue losses estimated at $2 million per year; Boeing has interconnected that network via satellite to locations in Kansas, Virginia, Pennsylvania, and elsewhere, generating Pacific Northwest Bell revenue losses estimated at $400,000 per year. *Id.* at A-5, 6, *reprinted in* J.A. 3101, 3130, 3131.

From its investigation, the Commission staff concluded:

> [W]hether or not local bypass is successful, operationally and economically, will be determined in the next three to five years. If the carriers are slow in responding to business users' needs and bypass proves viable during this period, there could be an irreversible swing to local bypass by a large sector of the Fortune 500—and by various government agencies as well.

Id. at 4, *reprinted in* J.A. 3101, 3104.

The FCC's view was informed by its staff's "effort[] to identify and understand bypass activities, technology and trends," *id.* at 1, *reprinted in* J.A. 3101, 3101, and by comments "numerous participants" made. *Access Order* ¶ 107, 93 F.C.C.2d at 274. These included Comments of Southern Pacific Communications Co. at 17-19, *reprinted in* J.A. 1729, 1743-45 (OCC describes its use of microwave radio facilities to bypass local telephone network for local portion of interstate calling); Comments of the Association of Data Communications Users at 18, *reprinted in* J.A. 1416, 1433 ("ADCU members are currently availing themselves of bypass technologies and will continue to do so as such technologies are further refined"); and Comments of the Western Union Telegraph Co. in Response to Fourth Supplemental Notice of Inquiry and Proposed Rulemaking at 23, *reprinted in* J.A. 1827, 1848 ("Western Union already has a growing

investment of over $100 million in local distribution facilities as part of a specific program to reduce its dependency on the Bell System") (hereafter, Western Union Comments). AT&T and the BOCs, we note, submitted an extensive study of bypass economics and technologies. Comments of BOCs and AT&T in Response to the Fourth Supplemental Notice of Inquiry and Proposed Rulemaking at 90-105, *reprinted in* J.A. 1436, 1525-40.

Petitioners characterize much of the bypass data the Commission gathered as anecdotal, and much of the discussion as merely theoretical. The FCC, it is true, had nothing in hand approaching a "definitive analysis." *See* Appendix F at 1, *reprinted in* J.A. 3101, 3101. But Congress has charged the Commission with responsibility to regulate in "a field of enterprise the dominant characteristic of which [is] the rapid pace of its unfolding." *National Broadcasting Co. v. United States*, 319 U.S. 190, 219 (1943). "[P]ure factual determinations" were not, and could not have been, made; the FCC's decision inevitably rested on "judgment and prediction." *FCC v. WNCN Listeners Guild*, 450 U.S. 582, 594 (1981). In light of the material available to the Commission, and the leeway the FCC has to make "deductions based on [its] expert knowledge," *FCC v. National Citizens Committee for Broadcasting*, 436 U.S. 775, 814 (1978) (quoting *FPC v. Transcontinental Gas Pipe Line Corp.*, 365 U.S. 1, 29 (1961)), we cannot indict the agency's assessment of the bypass risk as arbitrary or unsupported.

Petitioner NARUC and intervenor Rural Telephone Coalition (RTC) wanted the Commission to deal with uneconomic bypass by denying potential bypassers permission to construct facilities posing the problem. *Access Order* ¶ 110, 93 F.C.C.2d at 274 & n.38. The FCC rejected this proposal as unsound and unworkable. It stated:

> We are simply not in a position to determine what constitutes an uneconomic "bypass" service and what

> is a wholly new service that will attract a new set of users and enhance the ability of all users to make full use of telecommunications service-potential. For example, some comments assert that cellular services constitute a bypass technology. We have concluded, however, that cellular radio is a distinct service that serves distinct needs and that cellular service could be complementary to existing wireline service. Indeed, a given technology may be the efficient means of providing service to certain groups yet constitute uneconomic bypass for other services or groups.

Id. ¶ 111, 93 F.C.C.2d at 275. It was not unreasonable for the FCC to resist an approach that would curtail, and perhaps stifle, development and construction of new technology.[25]

According to intervenor Michigan, the Commission is disarmed by its own self-confessed inability to identify

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[25] NARUC and RTC invoked § 214 of the Act as empowering the Commission to act as these petitioners proposed. It appears, however, that the Commission's § 214 powers do not extend to entities other than common carriers. *See* 47 U.S.C. § 214 (1976).

California suggests that "the practical alternative to bypass lies not in prohibiting new services nationwide, but in [the states'] addressing the phenomenon as it actually arises in actual situations." California Brief at 17. To the extent California means the FCC should have remitted to the states the task of prohibiting construction of specific bypass facilities, the Commission appropriately refused to rely on local agencies to make technological judgments the Commission considered itself incompetent to undertake successfully. To the extent California means the state commissions should be left to address the bypass threat through "rate-making structures [that] provide for a reduced NTS payment by high-volume users" on a case-by-case basis, *see* Oral Argument Transcript at 65-68 (statement of Bruce Renard, counsel for Florida Public Service Commission), we again find the Commission's decision reasonable. The FCC could well conclude that it was unsound to address distortions in the interstate rate structure by introducing complementary distortions in the intrastate rate structure.

uneconomic bypass. Without any evidence of the existence of the phenomenon the FCC seeks to check, Michigan argues, the agency's position rests on quicksand. *See* Reply Brief of Intervenors the State of Michigan and the Michigan Public Service Commission at 2.

We have already underscored the permissibly predictive, judgmental character of the Commission's stance. *See supra* p. 47. The FCC sufficiently established the existence of bypass as a real market force. It sufficiently established both 1) the inability of regulators, under a noncost-based pricing system, to determine accurately the economic efficiency or inefficiency of a given technology, and 2) the likelihood that market participants under such a system will exploit available bypass technology when they can reduce their costs by doing so. *Cf.* Western Union Comments at 23, *reprinted in* J.A. 1827, 1848 ("To the extent that access charges are set at excessive levels, there can be little doubt that interstate users will be encouraged to invest in unnecessary and duplicative facilities. This is particularly true in the case of private line users, and Western Union is a case in point."). As a reviewing court, we would reach beyond our limited range of surveillance if we demanded more.[26]

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[26] Michigan argues similarly that no evidence supports the Commission's concern that pricing long-distance service above cost artificially represses usage. Brief of Intervenors the State of Michigan and the Michigan Public Service Commission at 7. Michigan notes the Commission's statement that it "ha[d] some questions concerning the methodology used in [one] study" of long-distance calling, and that it found "[c]ertain assumptions underlying the results of [another] study . . . questionable or unclear." *See Access Order* ¶ 112, 93 F.C.C.2d at 275 & n.39.

We do not see the Commission's recognition of flaws in studies it considered as tantamount to a rejection of those studies as worthless. The Commission's reference to "artificial[] restrict[ion of] calling patterns," *id.*, we further note, did not figure as a major item in its analysis.

Intervenor Florida Public Service Commission faults the FCC for failing to determine the *degree* to which the price of access to the local network can be set above cost before it will be in the interest of large-scale users to turn to uneconomic bypass. Florida Brief at 5-6. The Commission, however, is engaged in a continuing venture. It is now undertaking the investigation Florida presses. *See Further Reconsideration Order* ¶ 20, 49 Fed. Reg. at 7,812:

> We will also develop and analyze additional information with respect to the extent and dangers of bypass. . . . [W]e intend to use this additional information to design the transition plan. The end user charges at particular points in the transition should be low enough to avoid any adverse effect upon the universality of service and high enough to produce toll rate reductions that are sufficient to deter uneconomic bypass.

We note finally that the threat of uneconomic bypass entered the Commission's calculus not as a self-standing justification for the agency's decision but as a particular —albeit important—feature of the FCC's general concern that proper allocation of resources requires a pricing system consistent with the lessons "[e]conomics teaches us." *Access Order* ¶ 27, 93 F.C.C.2d at 251.[27]

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[27] One petitioner criticizes Commission reliance on economic theory in allocating the costs of access to the local exchange. California Brief at 15. California, however, has not persuaded us that "the generally accepted principle that recovery of fixed costs through usage charges impairs economic efficiency is not applicable to telecommunications," *Further Reconsideration Order* ¶ 11, 49 Fed. Reg. at 7,811, nor has it convinced us that economic efficiency is not a legitimate Commission goal.

Certain petitioners concede that "the Commission's decision to impose flat rates for NTS cost recovery follows logically from the perceived problems of discriminatory and preferential rates and uneconomic bypass," but argue that the agency has not justified "imposition of such flat rates on end users rather than on interexchange carriers." Brief of Intervenors Roseville Telephone Company, *et al.* at 23. Imposition of flat

b. Universal Service

We turn next to an objection of a different order. Intervenor RTC challenges the Commission's conclusion that a cost-recovery plan involving flat-rate end user charges will not have a substantial adverse impact on universal service. The only FCC decision now ripe for our review, however, is the agency's determination that *some* access costs should be recovered through end user charges. *See Further Reconsideration Order* ¶¶ 13-26, 49 Fed. Reg. at 7,812-13.

The FCC has deferred, pending further study, determination of the extent to which NTS subscriber plant costs should be shifted to residential end users. *See id.* ¶ 19, 49 Fed. Reg. at 7,812 ("additional information with respect to the elasticity of demand for local exchange service . . . will . . . assist us in determining the maximum charge that should be established at the end of the transition"). In ongoing supplemental proceedings, the Commission seeks "to devise an exemption for persons who cannot afford to pay any end user charge, reevaluate the transition plan for end user charges, and explore alternative mechanisms to assist customers of small telephone companies." *Id.* ¶ 4, 49 Fed. Reg. at 7,811.

The FCC has thus far made two firm, correlative determinations: (1) relying on its determination that "demand for exchange telephone service . . . is very inelastic," it has rejected claims that *no* end user charge can be levied without driving many exchange service subscribers away from the telephone system, *id.* ¶ 13, 49 Fed. Reg. at 7,812; (2) it has concluded that "[m]ost residential and single-line business customers can . . . afford to pay at least a portion of their Common Line costs through fixed charges," *id.* ¶ 15, 49 Fed. Reg. at

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rates on interexchange carriers, however, ultimately results in passing those costs on to end users on a usage-sensitive basis. A pass-on of that kind, if it became the final solution, would defeat the FCC's goal.

7,812. We see no sound basis for assailing these determinations as unreasoned or unsupported.

RTC relies primarily on L. Perl, Economic and Demographic Determinants of Residential Demand for Basic Telephone Service (1978). It argues that if the FCC adopts what has been known in this proceeding as a "Pure 2" plan, and if state regulators adopt similar schemes with regard to intrastate long distance rates, then nationwide telephone penetration could decline by as much as eight percent. Brief of Intervenor Rural Telephone Coalition at 7. "Such a decrease," RTC argues, "can hardly be said to be insignificant by an agency charged with maintaining service at reasonable rates 'to all the people.' " *Id.* at 7-8.

A "Pure 2" approach, however, would involve immediate recovery of *all* subscriber plant costs through flat-rate end user charges without any Universal Service Fund, transitional period, or exemption mechanism. The FCC has rejected that approach; it credited arguments that "Pure 2 would constitute a substantial step away from universal service." *Access Order* ¶¶ 120-22, 93 F.C.C.2d at 277-78.

In summary, the Commission at this juncture has decided no more than this: *some* end user charge for residential and single line business users should go into effect on June 1, 1985. The Commission had record support for the view that a charge could be imposed without substantial negative effect on universal service. *See Analysis of Effects of Federal Decisions on Local Telephone Service*, FCC 83-567 (released December 21, 1983). It has not decided the size of the charge, the shape of the transition, or the class of persons affected. When those decisions are made, RTC and other interested entities will be positioned to seek review of the precise plans the Commission adopts.

c. Alleged Procedural Deficiencies

Petitioners raise several procedural objections. NASUCA argues that notice-and-comment proceedings

did not suffice. Trial-type hearings were required, NASUCA maintains, because the Commission "prescri[bed] rates and revenue requirements." NASUCA Brief at 24.

In *AT&T v. FCC*, 572 F.2d 17, 21-23 (2d Cir.), *cert. denied*, 439 U.S. 875 (1978), the Second Circuit reviewed the FCC's prescription of unlimited resale and sharing of private line services; it found in the Administrative Procedure Act (APA) and Communications Act no relevant trial-type hearing requirement.[28] If *AT&T v. FCC* is the appropriate guide, we should end our inquiry here, for we have no authority to add to the procedural requirements ordered in the Communciations Act and the APA. *Vermont Yankee Nuclear Power Corp. v. Natural Resources Defense Council*, 435 U.S. 518 (1978); *see also Western Union Telegraph Co. v. FCC*, 665 F.2d 1126, 1151-52 (D.C. Cir. 1981).

NASUCA appears to urge separation of this case from *AT&T v. FCC* on two grounds. Even if the Act does not require trial-type hearings for Commission prescription of "practices" as in *AT&T*, NASUCA first suggests, it does require such hearings when "revenue requirements and rates" are at stake. *See* NASUCA Brief at 26 n.2 (emphasis omitted). Second, even if the Act itself does not require trial-type hearings before the Commission may prescribe rates, NASUCA states, "well-settled agency procedures of long standing" do so require; *Vermont Yankee*, NASUCA observes, does not impede judicial correction of an agency's "totally unjustified departure" from its own procedures. Joint Reply Brief of Petitioner NARUC, *et al.* at 27-28 (quoting *Vermont*

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[28] Additionally, the court viewed the Commission's action as involving promulgation of prospective rules to implement agency policy, not "adjudicat[ion of] disputed facts in particular cases" for which a trial-type hearing might be appropriate. 572 F.2d at 22 (quoting United States v. Florida East Coast Ry., 410 U.S. 224, 245 (1973)).

Yankee, 435 U.S. at 542). NASUCA points to cases in which the Commission has investigated the legality of carrier-filed rate increases, *see, e.g., In re AT&T*, 57 F.C.C.2d 960 (1976), determined a carrier's revenue requirements as part of an assessment of the legality of its charges, *see In re AT&T*, 9 F.C.C.2d 30, *modified*, 9 F.C.C.2d 960 (1967), or evaluated a carrier request to increase its prescribed rate of return. *In re AT&T*, 73 F.C.C.2d 689 (1979).

These arguments are not convincing. The Commission referred briefly at one point in its discussion to an "approximate[]" revenue requirement for interstate NTS exchange plant. *See Access Order* ¶ 25, 93 F.C.C.2d at 250. The rules it adopted "to determine the manner in which telephone companies will be compensated for the origination and termination of interstate and foreign communications services," *Further Reconsideration Order* ¶ 1, 49 Fed. Reg. at 7,810, included "many of the steps that carriers must follow in order to compute access charges," *Access Order* ¶ 43, 93 F.C.C.2d at 256, and some limited direct prescription of charges—for example, the $25 surcharge on private lines. But the FCC prescribed no specific revenue requirement and did not determine the legality of specific rates. On the contrary, the Commission initiated broad-gauged rulemaking to develop policies for the interstate long-distance market and it set prospective, policy-implementing rules.

Nor does longstanding FCC procedure chart the Commission's course in this extraordinary matter. There is no Commission case closely in point establishing a trial-type hearing pattern.[29] As the Commission observed five years ago:

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[29] We express no opinion on whether the Act or longstanding Commission policy calls for an evidentiary hearing where the Commission determines, for example, whether a carrier-filed rate is just and reasonable; that kind of case is not before us. *But see* Investigation of Access and Divestiture Related

> We have noted claims that evidentiary hearings will provide the most effective mechanism for accurate fact-finding. However, that type of multiparty proceeding could become almost interminable, given the complexity of the issues which we must resolve. We are endeavoring to establish an entry policy for the 1980's. A procedural option which would preclude us from reaching a final decision at or near the beginning of that decade would not be consistent with that goal.

MTS & WATS Market Structure: Supplemental Notice of Inquiry and Proposed Rulemaking, 73 F.C.C.2d 222, 232 (1979).

NASUCA stands on somewhat firmer ground in complaining that the Commission did not give the parties an immediate opportunity to comment on the staff study of bypass. The study was not released until the Commission reached its initial *Access Order* decision. We have more than once cautioned agencies "that even in an informal [proceeding] parties have a right to be informed of and comment on staff positions." *Independent United States Tanker Owners Committee v. Lewis*, 690 F.2d 908, 925-26 (D.C. Cir. 1982) ("[W]here an agency's analytic task *begins* rather than ends with a set of forecasts, sound practice would seem to dictate disclosure of those forecasts so that interested parties can comment on the conclusions properly to be drawn from them.") (emphasis in original); *see United States Lines, Inc. v. Federal Maritime Commission*, 584 F.2d 519, 534 (D.C. Cir. 1978) ("[W]e have required information in agency files or reports identified by the agency as relevant to the proceeding to be disclosed to the parties for ad-

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Tariffs, FCC 84-201, at ¶ 113 (released May 15, 1984) (resolving cost issues and determining the legality of rates through notice and comment proceedings; finding that parties received "the full opportunity for hearing required by Section 205(b) of the Act").

versarial comment. . . . Such requirements . . . ensure that parties to agency proceedings are afforded the opportunities guaranteed by statute meaningfully to participate in those proceedings . . . ."). Disclosure of staff reports allows the parties to focus on the information relied on by the agency and to point out where that information is erroneous or where the agency may be drawing improper conclusions from it. An agency's denial of a fair opportunity to comment on a key study may fatally taint the agency's decisional process.

But automatic upset should not attend a fault of the kind that occurred here. *See FCC v. WNCN Listeners Guild*, 450 U.S. 582, 591 n.22 (1981); *see also Air Transport Association of America v. CAB*, No. 83-1174, slip op. at 9-10 (D.C. Cir. April 20, 1984). Because the Commission gave this case reconsideration and further reconsideration, interested entities eventually had ample opportunity to address the staff study, and the FCC ultimately collected reams of comment. The bypass study should have been released earlier. The Commission's reconsideration decisions, however, were framed with adversarial comment in full view. Essentially, the error has been rendered harmless. *See Independent United States Tanker Owners Committee*, 690 F.2d at 926 (importance of allowing parties to comment on staff report "augmented" because of absence of opportunity for reconsideration); *United States Lines*, 584 F.2d at 535 ("While [disclosure of data and reports relied on by the agency] would ideally appear appropriate at the earliest stage of the agency proceeding, at the very least it is clear that it must come in the final decision so that reconsideration may be sought and judicial relief meaningfully afforded.").[30]

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[30] Intervenors Roseville Telephone Company, *et al.* claim that the Commission gave insufficient notice of its intention to impose a plan involving flat-rate end user access charges. Brief of Intervenors Roseville Telephone Company, *et al.* at 8-15. The Commission's request for comments, however, made it

3. *Centrex-CO Service*

Centrex-CO is a tariffed service sold by local phone companies. It offers such telecommunications functions as intercom calling, conference calling, direct inward dialing, and automatically identified outward dialing. *Reconsideration Order* ¶ 43, 48 Fed. Reg. at 42,991. These electronic switching services are performed at the exchange carrier's central office switch, and have traditionally been offered principally to large organizations and government agencies as an alternative to purchasing or leasing a private branch exchange ("PBX"), which is a smaller switch located on the subscriber's premises used to provide the same services. Because Centrex-CO switching is executed off-premises, each Centrex-CO subscriber station must be connected by a loop to the central office switch. Consequently, Centrex-CO service requires approximately six times more loops than PBX service, which primarily uses inside wiring to link together subscriber stations. Brief of Public Service Commission of the District of Columbia at 12.

The Commission ruled that Centrex-CO lines are generally subject to flat-rate per line access charges, as are other local loops between the subscriber's premises and the local switch used jointly in exchange and inter-

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clear that the Commission was considering an approach under which "[e]very customer . . . would pay a flat (per line) access charge that did not vary with use, plus usage based interstate charges that reflected only usage sensitive facilities . . . plus local charges." MTS and WATS Market Structure: Fourth Supplemental Notice of Inquiry and Proposed Rulemaking, 90 F.C.C.2d 135, 140 (1982). The Commission described this approach as "extremely attractive" from the point of view of "equity between services and economic efficiency," but expressed concern about its effect on universal service. *Id.* at 140 & n.10. Moreover, the Commission detailed a second approach also involving "flat-rate access charge[s]," *id.* at 142-44, and requested comment on the bypass issue. *Id.* at 145-47.

exchange traffic. This ruling effectively imposed substantially higher total access charges on Centrex-CO service, potentially rendering it significantly less economical to subscribers than its principal competitor, PBX. Several parties now seek to overturn the Commission's decision. Some, such as the Public Service Commission of the District of Columbia ("D.C.P.S.C.") argue that the Commission treated Centrex-CO subscribers too harshly, threatening the very existence of the service; others, representing the PBX industry, claim that the Commission granted an unlawfully discriminatory preference to Centrex-CO service.

The D.C.P.S.C. claims that the Commission should not have applied a full per line access charge to existing Centrex-CO systems. It argues that the per line fee should be set at only sixteen percent of that levied on other local loops in order to maintain competitive parity with PBX. *Id.* at 28-29. Failure to levy the access charge in this manner will allegedly cause a large number of subscribers to abandon Centrex-CO service, which in turn could threaten universal service since higher phone rates would have to be charged to the remaining exchange subscribers to recover the cost of the prematurely abandoned Centrex-CO plant remaining in the rate base. The D.C.P.S.C. charges that the Commission inadequately considered this problem of "stranded investment."

However, on the record before us we conclude that these arguments are without merit. The Commission thoroughly considered the objections of the D.C.P.S.C. and other similarly aligned parties below. Although it was generally unwilling to set access rates at a level which would not recover the full cost of Centrex-CO loops, it accepted the claims of state commissions that in many exchanges Centrex-CO rates may have been set above cost in order to subsidize local rates. Since a sharp rate increase in those circumstances could deprive the

telephone companies of a fair opportunity to adjust local Centrex-CO rates downward to compensate, depriving customers of any benefits that might be derived from efficiently priced, economical Centrex-CO service, the Commission decided to adopt partially the suggestions made by the D.C.P.S.C. It ruled that the full multi-line business access rate will be applied only prospectively, to newly laid Centrex-CO lines. Existing Centrex-CO plant will be subject to transitional access charges, not to exceed $2.00 in 1984. *Reconsideration Order* ¶¶ 47-49, 48 Fed. Reg. at 42,991-92. These charges will be reexamined in supplemental proceedings and will presumably eventually be equivalent to the multi-line business access rate, but the Commission does not expect the access charge to exceed $3.00 in the 1985-1986 access period. *Further Reconsideration Order* ¶ 40 n.24, 49 Fed. Reg. at 7815.

The D.C.P.S.C. claims that this solution did not adequately address the potential threat to universal service since there was no record support in favor of the Commission's minimal predictions of stranded investment. In particular the D.C.P.S.C. argues that the rate structure prescribed within its jurisdiction provides subsidies to Centrex-CO from other classes of subscribers, not vice versa. However, the Commission did not base its conclusions on a finding that *all* local Centrex-CO exchange rates were subsidized, nor was it required to do so.

The Commission made other findings supported by record evidence which rationally buttressed its conclusion that there is no "threat to universal service so substantial and so imminent that we must depart from this approach. . . ."- *Id.* at ¶ 47, 49 Fed. Reg. at 7816.

First, the Commission recognized that as a practical matter most Centrex-CO users would be unable to terminate Centrex-CO service immediately. Several parties before the Commission indicated that it would take at least three years to move to alternative services. During

that interim period more costs of existing Centrex-CO plant could be recovered.

Second, testimony before a state commission cited by the parties indicated that a large percentage of Centrex-CO plant could be reused in other local service. *Id.* at ¶ 46. This further diminished the likelihood that universal service would be greatly impaired by full flat-rate per line access charges on Centrex-CO subscribers.

Third, the Commission took affirmative steps to monitor the threat posed by increased Centrex-CO rates. In the *Reconsideration Order* it requested the Joint Board in Docket 80-286 (1) to assist the Commission in monitoring "the nature and magnitude of any stranded investment problem," and (2) to recommend solutions which could be adopted at the state or federal level to avoid a threat to universal service. *Reconsideration Order* ¶ 49, 48 Fed. Reg. at 42,992. These were reasonable responses to the claims of the D.C.P.S.C. In view of the Commission's decision to refer this problem to the Joint Board, arguments of the D.C.P.S.C. that local rate payers will inevitably bear the full brunt of obsolescent Centrex-CO plant are premature.

The D.C.P.S.C. does not even offer a reasonable alternative to this decision. Permanent depression of Centrex-CO access charges to reflect only sixteen percent of the standard flat-rate end user charge in order to achieve parity with PBX users is inconsistent with the basic principles of the Commission's orders, which generally require end users to bear the cost of the interstate NTS charges attributable to their use of the exchange. The price disparity between Centrex-CO and PBX service is directly related to the *cost* of providing the exchange access. Because Centrex-CO requires approximately six times the number of local loops as PBX, the interstate share of local NTS costs is correspondingly higher. Access charges that rationally reflect that increased level

of costs are not discriminatory. *Id.* ¶ 45, 48 Fed. Reg. at 42,991. Pricing telecommunications services based solely on maintenance of comparative competitive positions, regardless of the cost of providing the services, would fundamentally contradict the primary rationale underlying the access charge proceedings. The Commission reasonably determined to apply these principles consistently to all end users, including Centrex-CO subscribers; we may not arbitrarily overturn that decision in our appellate review.

As might be expected, the PBX industry, as the principal competitor of Centrex-CO service, supports the Commission's decision to impose full flat-rate end user access charges on Centrex-CO service. However, represented by the North American Telecommunications Association ("NATA"), a trade association comprised of manufacturers, distributors, retailers, and installers of customer premises equipment, the PBX industry challenges the Commission's authority to grant *any* transition to Centrex-CO users. NATA's argument is two-pronged.

First, it asserts that the Commission's response to the threatened loss of competitive Centrex-CO equipment was not supported by record evidence. NATA argues that instead of relying on representations made by the state commissions and other commenting parties the Commission should have amassed the relevant underlying facts, and then independently analyzed them to develop its own conclusion on the level of intrastate Centrex-CO costs, and the concomitant effect on local rates and universal service of immediate Centrex-CO rate hikes. Brief of Petitioner/Intervenor NATA at 58. Failing to complete these steps, NATA charges that the Commission has not presented "the minimum of evidence upon which an agency can rely to support agency action in an informal . . . rulemaking." Reply Brief of Petitioner/Intervenor NATA at 12.

Second, NATA charges that the lower transitional rates charged to Centrex-CO subscribers unreasonably discriminate against all other classes of business end users since the price discrepancies are not cost based. The proper remedial action, NATA urges, is to "direct the Commission" to eliminate the transitional preference for Centrex-CO users. Brief of Petitioner/Intervenor NATA at 45. However, neither of NATA's arguments would justify such an order to the Commission.

An agency decision arrived at through informal rulemaking must have a rational basis in the record and be based on a consideration of the relevant factors under its statutory mandate. *Almay, Inc. v. Califano*, 569 F.2d 674, 681 (D.C. Cir. 1977). Consequently, when an agency undertakes a thorough, primary, evaluation of all relevant facts, it is highly desirable that the agency: independently amass the raw data; verify the accuracy of that data; apply that data to consider several alternative courses of action; and reach a result confirmed by the comments and submissions of interested parties. But the Commission's failure to take or complete some of these steps does not fundamentally prejudice its decision. The paradigmatic scope of agency expertise is often pragmatically circumscribed *internally* by limited agency resources and restricted *externally* by the need to respond to complex, growing regulatory problems within a reasonable period of time. Notice and comment procedures are partially designed to overcome this problem. They permit parties to bring relevant information quickly to the agency's attention. A degree of agency reliance on these comments is not only permissible but often unavoidable. Thus, although an agency must consider and analyze the factual materials gathered during the informal rulemaking process, *see Action for Children's Television v. FCC*, 564 F.2d 458, 471 (D.C. Cir. 1977), we have never held that an agency must conduct this analysis without relying on the comments submitted during the rulemaking.

In a lengthy and complicated rulemaking such as this one it could very well be impossible to conduct elaborate independent verification proceedings on each factual comment submitted to the agency and still conclude the proceeding within a reasonable period. The Commission implicitly recognized the difficulty of immediately conducting a complete assessment of the local tariffs for Centrex-CO service when it chose "to delay the full impact of the new rate structure until state commissions could reevaluate the rate structures for Centrex-CO services . . . and to allow time for the Joint Board to study the subject." *Further Reconsideration Order* ¶ 50, 49 Fed. Reg. at 7817. The Commission's decision to rely on the comments of the state commissions that some Centrex-CO services are priced above cost, pending a more thorough assessment of the problem, was a reasonable response.

The representations made by various parties, including the Bell Operating Companies and state commissions, contained specific allegations about the impact on local Centrex-CO rates that could cause tens or hundreds of millions of dollars of equipment to be idled. *See* Brief of Intervenors Bell Operating Companies at 69 nn. 81-82. State commissions and other commenters also argued that Centrex-CO rates were set above cost to subsidize residential rates. The Commission was entitled to rely on these representations by parties who were uniquely in a position to know the level of current subsidization and the impact on local rates of nongraduated Centrex-CO access charges.

This is not a case in which party submissions were accepted uncritically by the Commission. On the contrary, the FCC rejected a number of petitions as "unsupported speculation" and criticized other more substantially grounded estimates of revenue loss. *Further Reconsideration Order* ¶ 46, 49 Fed. Reg. at 7816. However, the Commission was unwilling totally to discount the prob-

lems which could be posed by stranded Centrex-CO investment. It requested the Joint Board to monitor the situation. The Commission also understood several responsible petitioners to assert the existence of above-cost Centrex-CO pricing, supporting the conclusion that an interim period would be necessary to permit some state commissions to reevaluate their Centrex-CO tariff policies. The decision to accommodate that period of reevaluation, in conjunction with the establishment of a Joint Board, was the method chosen by the Commission to balance the risks and benefits alleged to follow its regulatory action. That balancing, based on the Commission's expert evaluation of the comments placed before it, is reasonable and rationally supported by the record.

NATA's argument that the Commission has unreasonably discriminated between Centrex-CO and PBX subscribers is also without merit. The Commission is quite properly concerned about facilitating the capacity of state regulators to respond meaningfully to its orders, and minimizing unnecessary disruptions in service. A transition period to full implementation of Centrex-CO access charges is rationally related to those goals and is in no way unlawfully discriminatory.

The Commission very carefully threaded its way through the opposing claims raised by local exchange companies and the PBX industry, evaluating the sufficiency of those comments, and responsively adjusting its access orders to achieve what it determined in its expert discretion to be the optimum balance among its statutory goals. The decision to impose flat-rate Centrex-CO access charges on a per line basis after a period of transition is supported by the record and reasonably related to those goals. We affirm the FCC's conclusions on this issue.

4. *Party Lines*

In addition to prescribing special rules for end users of Centrex-CO systems, the Commission also considered

the proper structure of party-line end user access rates. Unlike ordinary subscription service, in which one loop serves only one subscriber, party lines permit several subscribers to share a single loop, reducing the cost of the telephone service to each subscriber. The service is often used in rural areas where the average cost of laying each loop may be much higher than in urban exchanges.

In its *Access Order* the Commission directed that the access charge for individual party-line subscribers be computed by dividing the standard access fee for a single-subscriber loop by the number of party-line subscribers sharing the party line. *Access Order*, App. A., 47 C.F.R. § 69.104(c), 93 F.C.C.2d at 349. On reconsideration, several parties claimed the rule would be too burdensome to administer on a line-by-line basis. In response the Commission adhered to its decision to compute the charge by dividing the single-line rate by the number of party-line subscribers, but permitted the number of subscribers to be calculated based on the average level of subscription, or "fill," in each class of party-line service, such as two-party, four-party, or six-party lines, rather than individually tallying the number of subscribers to each party line. *See Reconsideration Order*, App. A., 47 C.F.R. § 69.104(c), 48 Fed. Reg. at 43,018.

The Rural Telephone Coalition ("RTC") charges that the Commission acted unreasonably in adopting this system. It claims that this system inaccurately reflects the cost of providing party-line service, since party lines do not cost less in direct proportion to the number of subscribers sharing the line. Record evidence relied upon by RTC suggests that a multiple line system serving several subscribers with separate loops may cost only 25% more per subscriber than a party-line system, although the Commission's rules would impose an access charge on a single-line subscriber up to 250% greater than that paid by the party-line subscriber. Petition for Reconsideration and Clarification of the RTC, J.A. 2926, 2941-42,

2958. Because the proposed system thus "misstate[s] the relationship between the cost of providing party line and single party service," Brief of Intervenor RTC at 19, single-line subscribers effectively subsidize much of the cost of providing the inferior grade party-line service. The RTC argues that this distortion between cost of party-line access and the assigned flat-rate charge would create an artificial economic incentive for customers to switch from single-line to party-line service. Besides artificially encouraging the widespread use of a lesser grade of service, the RTC asserts that the cost of converting existing single-party plant to party-line plant would cost more than building single-line plant initially.

The Commission failed to respond adequately to these charges. Its *Reconsideration Order* recognized that the RTC objected to the "uneconomic incentives for choosing party-line over single-line service." *Reconsideration Order* ¶ 38, 48 Fed. Reg. at 42,990. The Commission also agreed with the RTC that end-user party-line charges are intended to reflect the actual cost of providing the service. However, the Commission never responded to the RTC's comments and evidence suggesting that the party-line plan established by the Commission contradicts these very goals.

The Commission made two modifications to its party-line plan on reconsideration. First, it required computation of the fill ratio for each class of party-line service, rather than for each line. However, far from "largely ameliorat[ing] the problems perceived by" the RTC, *id.* ¶ 39, this amendment addresses only the method of administering the plan, not the cost-price relationship between single and party-line service. The Commission's second change, waiver of its party-line allocation rules in those rare cases when party-line service may cost more to provide than single-line service, is similarly nonresponsive to the core problem identified by the RTC: as a general rule the cost of party-line access per subscriber will not

be recovered by that subscriber's access charges, even when that party-line costs *less* than a single-subscriber line.

The only record evidence on the issue of party line costs was that submitted by the RTC which suggested that interstate party-line access charges would *not* fully reflect costs. The Commission never referred to this evidence, never explained why it was flawed or unreliable, and never offered any alternative explanation for its plan. It is thus entirely likely that the Commission unwittingly adopted a party-line plan totally inconsistent with the driving principle behind its access charge decisions, which is to align the level of access charges, as far as possible, with the actual cost of access.

Certainly the Commission would not be required to maintain full cost-based access pricing for end-user party-line charges, but we should expect to find either a clear explanation for its departure from the general principle followed elsewhere in the rulemaking, or a responsive rebuttal of charges that its party-line access charges do not accurately reflect costs. The Commission offered neither. It concluded its discussion in apparent agreement with the RTC that party-line charges should permit rational economic choices, again ignoring the RTC's claim that the Commission's plan would reach the opposite result.[31] This unexplained and unsupported conclusion is the antithesis of rational rulemaking.

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[31] The Commission stated:

> We are sympathetic to the Rural Telephone Coalition's concern that party-line service is an inferior grade of service that may deny many customers the benefits of more advanced communications services. Nevertheless, we believe that these customers will be able to decide whether the benefits to be gained from single-line service are worth the added costs. Interstate access charges that reflect costs will permit their choice of single or party-line service to be a rational one.

Reconsideration Order ¶ 41, 48 Fed. Reg. at 42,990.

We must therefore remand this portion of the Commission's orders for meaningful consideration of claims that its party-line access charges are uneconomically subsidized by single-line access rates. Further analysis by the Commission, accompanied by a well-articulated explanation of its response to these claims will, we are confident, clear up the confusion that now exists about the extent to which end-user party-line access charges are intended accurately to reflect the cost of providing the service and the extent to which party-line access fees actually achieve their intended result.

5. *Average Schedule Company Status*

The last major part of the Commission's rules dealing with end-user access charges challenged in this proceeding concerns not *who* will bear the charges, but the method by which smaller exchange companies will identify the level of their costs incurred in providing access. Before an exchange carrier can recover its access costs, it must first determine what they are. Precise determination of a local company's costs in all relevant areas may require extensive data collection, analysis, reporting, and auditing, which can be a difficult and costly burden for small telephone companies. As a result, the Commission's rules have traditionally allowed smaller exchange carriers to estimate some or all of their costs through use of an "average schedule" which adopts generalized industry data to reflect the costs of a hypothetical exchange company. According to the RTC, many of the small exchange carriers which elect to use the average schedule, known as "average schedule companies," use the average schedule to compute every element of their costs except the expense of connecting local central offices to toll offices, or "line haul" costs. Because line-haul cost studies are relatively less expensive and less complicated than procedures necessary to identify other types of costs,

a large number of smaller exchange companies prefer to conduct their own rather than rely on the average schedule.

The FCC, in the access orders, changed current practice relating to average schedule company status in two ways. First, the Commission ruled that a company may no longer elect to use the average schedule if it is affiliated with, or owned by, a carrier computing its costs directly, often referred to as a "cost company." *See Reconsideration Order*, App. A., 47 C.F.R. § 69.605(c)(1), 48 Fed. Reg. at 43,022. Second, the Commission required that companies electing average schedule status participate in all of the general exchange carrier association tariffs, effectively precluding a carrier from using independently generated cost data to demonstrate line-haul costs while relying on the average schedule to establish all other costs. *Id.* ¶ 193, 48 Fed. Reg. at 43,014; *Access Order*, App. A., 47 C.F.R. § 69.605(c)(2), 93 F.C.C.2d at 362. The RTC challenges both of these rules.

In reviewing the reasoning used by the Commission to support its decision to preclude partial reliance on average schedule status, it is again apparent that the Commission agreed with the fundamental objectives advanced by a commenting party, but promulgated a rule which could cause drastically different consequences, without record support for the discrepancy between means and end. The Commission clearly expressed its intent "to avoid imposing the burden of developing cost information upon companies" which may be too small to perform the necessary cost studies, *Reconsideration Order* ¶ 194, 48 Fed. Reg. at 43,014, a goal also advocated by the RTC. The Commission's decision is a substantial change from prior practice; the Commission recognized that many independent companies will be forced to abandon average schedule status. *Id.* ¶ 193. However, there is nothing in the record which suggests that parent, subsidiary, or affiliate status accurately distinguishes between those com-

panies which would be prohibitively burdened by the cost, and those which could easily bear it.

In defense of its rule the Commission reasoned:

> Some companies that are large enough to compile cost information undoubtedly also participate in average schedule settlements. We could not reasonably defer the implementation of access charges to identify such companies, but we *did* infer that companies or affiliated groups of companies that are partly in and partly out of average schedule settlements are not too small to perform cost studies.

Id. ¶ 194. Yet, the mere *inference* that affiliation alone indicates ability to bear the cost burdens of the affiliate is not always reasonable since, as the RTC argues, a small cost company affiliated with a second, small, average schedule company would not necessarily have sufficient financial resources to bear the full expense of dual, full-fledged cost studies. Reply Brief of Intervenor RTC at 7-8. More importantly, the Commission imposed this "compulsory pooling requirement," *Reconsideration Order* ¶ 193, 48 Fed. Reg. at 43,014, between affiliates without inquiring into the regulatory or corporate barriers which may prohibit such cross-pooling; in particular, the RTC argues that state commissions may not allow revenues of locally regulated exchange companies to be diverted to fund the operations of affiliated companies in other jurisdictions. Reply Brief of Intervenor RTC at 8.

The Commission dismissed similar arguments below without any explanation, asserting that the average schedule companies have "not presented any reason for concluding that they should be entitled to" the benefits accruing from their current average schedule status. *Reconsideration Order* ¶ 195, 48 Fed. Reg. at 43,014. This minimal consideration is inadequate, especially since the Commission came close to accepting the weight of these arguments when it decided to delay the start-up date of

the new rule for two years.[32] However, a transition period alone does not mitigate the difficulties identified by the RTC, since it fails to address the reasonableness of the Commission's inference that cost companies are generally both financially prepared and administratively authorized to bear the cost burdens of affiliated average schedule companies. We are therefore remanding this aspect of the *Access* orders to the Commission for further study and consideration on these issues.

Given the Commission's willingness to defer the effective date of this rule for two years, our remand to the Commission for a brief period to enable the Commission to conduct a more responsive and meaningful evaluation of small carriers' claims does not run counter to the Commission's stated desire to avoid unreasonably deferring the implementation of access charges pending the identification of those carriers who are currently able to compile individualized cost information. It will ensure that the Commission, otherwise spurred by the necessity to design and establish a comprehensive access charge plan at the earliest reasonable date, does not give short shrift to the complaints of small exchange companies that the benefits historically derived from the existing average schedule company status rules would be lost by the unconsidered decision to abandon the prior rules in favor of a less reasonable system not immediately necessary.

For similar reasons we must also remand this proceeding to the Commission for a reasoned evaluation of the parties' challenge to the Commission's refusal to permit use of average schedules for less than all access costs. The Commission announced this new rule in its *Access Order* without any prior public notice or opportunity for participation by the affected parties. Its reevaluation of

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[32] The Commission noted, "[i]t may be difficult for such affiliates [of cost companies] . . . that are presently compensated as average schedule companies to develop cost data." *Reconsideration Order* ¶ 195, 48 Fed. Reg. at 43,014.

the rule in light of the substantial comments subsequently submitted in petitions for reconsideration demonstrates a failure to consider seriously the legitimate objections of small exchange companies.

The RTC has identified at least one significant reason which could justify softening of the new rule: forcing exclusive reliance on the average schedule could gravely affect companies with exceptionally high line haul costs. Brief of Intervenor RTC at 17. Computation of these costs, unlike other categories of access costs, can be done through relatively simple accounting procedures. Reply Brief of Intervenor RTC at 10. In its *Reconsideration Order* the Commission merely added conclusory language without addressing these contentions. The FCC's explanation for the rule change reads in full:

> Some petitioners also note that the existing average schedule system gives a company the option of participating in an average schedule for only a portion of its costs and suggest that the access charge rules be modified to include such an option. The average schedules do not appear to correspond with access elements we have defined and accordingly could not be easily adapted even if we found that such a system would be desirable.

Reconsideration Order ¶ 196, 48 Fed. Reg. at 43,014.

However, it may be possible that the newly reorganized categories, or "elements," *see id.* ¶ 4, 48 Fed. Reg. at 42,985, of access costs can be harmonized with the established industry practice in this area, or that the average schedules can themselves be adjusted to reflect the new access cost elements identified by the Commission. Reply Brief of Intervenor RTC at 9-10. The Commission never adequately considered these possibilities.

By ignoring these alternatives and the potential advantages to continuing the status quo, the Commission failed to discharge its special responsibility to balance

the policies embodied in the Communications Act, selecting the regulatory course of action most likely to meet the public interest. Accordingly, the Commission's orders prohibiting election of partial average schedule company status are remanded to the Commission for further consideration.[33]

B. *Access Charges to Carriers and Private Line Users*

Not all of the interstate share of local exchange costs will be recovered through flat-rate end user access fees. Traffic sensitive exchange costs will be recovered from interexchange carriers on a usage sensitive basis. *See Access Order* ¶¶ 197-249, 93 F.C.C.2d at 297-315. The Commission established an additional component of the carrier's access charges which is designed to recoup costs assigned to the "carrier common line element," including (1) the NTS costs associated with inside wiring and customer premises equipment, (2) the gradually declining balance of local NTS exchange costs not recovered from end users pending the transition to more fully cost-based end user access charges, and (3) the cost of the Universal Service Fund established to help subsidize certain NTS costs on a permanent basis. Only the Universal Service Fund is expected to be a nontransitional component of the carrier common line element. The inside wiring and customer premises equipment costs will be gradually removed from the rate base, and the balance of NTS exchange costs not recovered from end users or through the Universal Service Fund will probably drop to zero. Brief for FCC at 30 n.46, 31 n.47.

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[33] We note that this analysis can apparently be completed without jeopardy to the efficient, smooth implementation of the Commission's orders, since the Commission has waived the requirement that companies elect between cost and average schedule status pending the modernization of average cost schedules. MTS and WATS Market Structure, 49 Fed. Reg. 10,549 (1984).

The costs allocated by the Commission to the carrier common line element will be recovered on a usage sensitive basis from most interexchange carriers in the form of a carrier common line charge. *See id.* at 30. A private line surcharge intended to approximate the carrier usage charges will be levied on private line users and a few other classes of specialized carriers. *See Reconsideration Order* ¶ 81, 48 Fed. Reg. at 42,997; *id.* App. A., 47 C.F.R. § 69.115(b), 48 Fed. Reg. at 43,019. In this section of the opinion we discuss claims raised by the affected carriers and private line users that the Commission acted unlawfully when it assigned these access charges to the various categories of exchange users.

1. *Unlawful Discrimination Against Carriers Subject to the Carrier Common Line Charge in Favor of Other Interstate Users of Exchange Facilities*

The advent of competition in the provision of interexchange telephone services, and the rapidly proliferating varieties of services offered through the medium of telephone transmissions, demonstrated to the Commission the need for a coherent, uniform method of compensating exchange carriers for the interstate costs of providing exchange access. The correction of disparities in exchange access rates charged to the various classes of interexchange carriers was a primary goal in Docket No. 78-72. *See MCI Telecommunications Corp. v. FCC*, 712 F.2d 517, 529, 531-32 (D.C. Cir. 1983). The Commission asserts that it accomplished this result through the imposition of the usage-based carrier common line charge, *Access Order* ¶ 51 n.20, 93 F.C.C.2d at 258, and the private line surcharge. MCI disputes this claim. Before evaluating the merits of MCI's arguments we find it helpful to review briefly the effect of the Commission's orders on the previous system of exchange access compensation.

a. The Previous System of Exchange Access Compensation and the Commission's Response

In addition to AT&T, the predominant interexchange common carrier, several types of communications carriers and telecommunications consumers require access to the local exchange.

One category, composed primarily of commercial, specialized common carriers, offers to transport subscribers' telephone traffic between the originating and terminating local exchanges. Because this general type of service exists to provide interexchange carriage, virtually all interstate calls carried are accessed into the originating and terminating exchanges. Carriers offering this service include the *OCCs*, which use privately owned facilities to carry interexchange traffic for a basic fee; *resellers*, which lease OCC or AT&T interexchange facilities in order to offer high volume discounts to subscribing groups of moderately heavy interstate callers; and *sharers*, who join together in a nonprofit arrangement to use jointly the services and facilities of a single underlying carrier, paying a pro rata portion of costs based on relative use. *FX service* is another type of interexchange offering in which subscribers terminate all of their interexchange calls by switching them into the exchange, in this case by integrating the open end of the system into the distant exchange.

A second grouping of interexchange telecommunications users generally makes much more limited use of exchange access. These are the access users which the Commission identified as primarily responsible for the "*leaky PBX*" problem. They lease or own dedicated private lines used to provide point-to-point service, but terminate those lines at PBX facilities or other private switches that can patch an interstate private line call into the local exchange. Although the caller is thus able to originate and terminate jurisdictionally interstate calls, incurring interstate exchange costs, those costs are not currently

recovered from the private line subscriber since local exchange companies generally are not equipped to distinguish between the local and jurisdictionally interstate traffic routed to or from the PBX. In addition to private lines, some not-for-hire privately owned telecommunications systems, used by large corporations to provide voice and specialized data transmissions, are also capable of accessing the local exchange.

These private line arrangements are technically capable of switching the same volume of traffic into the local exchange as the exchange carriers in the first grouping. However, less intensive use of exchange access can probably be inferred, if only because the first grouping of services exists primarily, and is commercially offered, for the purpose of originating and terminating interexchange traffic on the local exchange, while the second grouping of services has traditionally been offered for the primary purpose of completing intrasubscriber telecommunications.

Of course, the lines between these two groupings of exchange access users are often blurred. The Commission recognized that "[d]epending upon the nature of its operation, a given private line . . . user may or may not make significant use of local exchange service for interstate access." *Reconsideration Order* ¶ 78, 48 Fed. Reg. at 42,996. One class of carriers which does not fit conveniently into either of these groupings is that of the *enhanced service providers*. These carriers use interexchange facilities to transport subscribers' data transmissions between computer or data terminals in different exchanges, and may rely heavily on access to the local exchange to originate or terminate their transmissions.

Regardless of the amount of use, each of these classes of carriers and private line users relies on technologically similar access facilities to originate or terminate calls in the local exchange. Prior to the Commission's orders un-

der review there was no uniform scheme through which these exchange users compensated the local exchange for the interstate share of NTS costs associated with their access. Through the settlements and division of revenues process the Commission has traditionally authorized a fairly high charge for exchange access on AT&T, which AT&T recovered through usage-based charges for ordinary long distance phone service. OCCs were subject to ENFIA rates, which included a negotiated discount from the access charge rate paid by AT&T. FX users paid only local exchange rates for their open end access, but have not borne any of the cost burden attributable to their interstate use of the exchange. Users of private lines capable of switching into the local exchange similarly paid only local rates. Thus, although the Commission determined that these private systems "originate and terminate vast quantities of interstate and intrastate toll traffic through the use of exchange telephone service," *id.* ¶ 80, under the access scheme in effect prior to its orders, "no charge whatsoever [was generally] assessed for interstate use of local services." *Id.* ¶ 81.

In surveying that system, the Commission found,

> [N]one of the participants has attempted to demonstrate that there is any reasonable or rational relationship to justify the wide disparities among the charges for access that are directly or indirectly levied upon users of the various interstate services that might satisfy the requirements of Section 202(a). It is readily apparent that it would be impossible to do so. Indeed, the current methods of recovering costs of jointly used non-traffic sensitive subscriber plant . . . are totally different and produce widely differing results even though each service uses the same plant in the same manner. . . . Since no one has attempted to justify the disparate rates charged for like access services in this proceeding, we must find them to be unlawfully discriminatory.

Access Order ¶ 51, 93 F.C.C. 2d at 258.

To remedy this discrimination the Commission ruled that users of exchange access generally must pay either a carrier common line charge or a private line surcharge to contribute towards the access costs not recovered from end users. The carrier common line charge applies to those carriers whose previous access rates were governed under the ENFIA tariffs. Carriers in this category include the OCCs, and many resellers. *Reconsideration Order* ¶ 83, 48 Fed. Reg. at 42,997; *id.* App. A, 47 C.F.R. § 69.105(a), 48 Fed. Reg. at 43,018. In addition, the Commission determined that FX users would also be subject to the carrier common line charge. The private line surcharge applies to most other users of interexchange telecommunications facilities which are capable of using local exchanges to originate and terminate these calls. Carrier groups subject to this "special access" surcharge are most private line users, sharers, and enhanced service providers. *Reconsideration Order* ¶ 83, 48 Fed. Reg. at 42,997; *id.* App. A., 47 C.F.R. § 69.115, 48 Fed. Reg. at 43,018, *as amended by Further Reconsideration Order*, App. A., 49 Fed. Reg. at 7829. One narrow class of exchange users, private communications systems, were not placed in either category, but are subject to reasonable non-discriminatory tariffs for exchange access which may be developed by local exchange companies in the future. *See Further Reconsideration Order* ¶¶ 130-33, 49 Fed. Reg. at 7826.

Both the carrier common line charge and the private line surcharge are based on relative use, but different methods are used to determine the amount which the carrier uses the local exchange to originate or terminate interstate calls. The carrier common line charge is tied to *measured* usage. OCCs will pay a flat, per line rate based on the projected relative use attributable to the average OCC line. *Reconsideration Order*, App. A., 47 C.F.R. § 69.105, 48 Fed. Reg. at 43,018, *as amended by Further Reconsideration Order*, App. A., 47 C.F.R. § 69.105(b), 49 Fed. Reg. at 7829. Resellers will be sim-

ilarly charged. FX users will pay a nonaveraged per minute/per line charge according to the actual use of each FX line. *See Further Reconsideration Order* ¶ 98, 49 Fed. Reg. at 7922. In a subsequent proceeding the Commission exempted FX lines whose use of the exchange cannot currently be measured. Pending development of measurement capability, these FX subscribers will pay only the local exchange rate or an alternative usage surrogate proposed by exchange carriers. *See Investigation of Access and Divest. Related Tariffs*, 49 Fed. Reg. 9174, 9185-86 (1984); Brief for FCC at 82 n.108.

Those subject to the private line surcharge pay a flat monthly fee of twenty-five dollars based on the *estimated* average per line use of exchange facilities. This surcharge is based on estimated rather than measured use primarily because local exchanges are not physically equipped to monitor the interstate usage of these special access subscribers. *See Reconsideration Order*, App. A., 47 C.F.R. § 69.115, 48 Fed. Reg. at 43,019, *as amended by Further Reconsideration Order*, App. A., 49 Fed. Reg. at 7829.

b. Failure to Cure Pre-existing Discrimination

Petitioner MCI claims that the Commission merely perpetuated the unlawful discrimination which the Commission found to exist in its *Access Order*, without curing the disparate charges for functionally similar access. MCI estimates that it will pay approximately $355 for each access line, while private line users will pay only the $25 surcharge. Because the two classes of telecommunications users utilize "the same plant in the same manner" but continue to pay widely divergent per line charges, MCI argues that the Commission merely continued the "widely different" rate results which originally caused the Commission to reach a finding of unlawful discrimination. *See Access Order* ¶ 51, 93 F.C.C.2d at 258. MCI seizes on the Commission's characterization of the plan as "designed to achieve a rough equity among

access service users," *Reconsideration Order* ¶ 77, 48 Fed. Reg. at 42,995, as proof that the Commission has breached its admitted obligation to develop a permanent solution to the "rough justice," *MCI Telecommunications Corp. v. FCC*, 712 F.2d 517, 524 (D.C. Cir. 1983), in access rates established in the ENFIA agreement. Brief for Petitioner MCI at 45-46. MCI demands that the unlawful discrimination be promptly remedied, relying on authority which prohibits the establishment or continuation of charges which have been held to be discriminatory or unlawful. *MCI Telecommunications Corp. v. FCC*, 712 F.2d 517, 535 (D.C. Cir. 1983); *National Ass'n of Motor Bus Owners v. FCC*, 460 F.2d 561, 568 (2d Cir. 1972); *American Trucking Ass'ns, Inc. v. FCC*, 377 F.2d 121, 130 (D.C. Cir. 1966), *cert. denied*, 386 U.S. 943 (1967).

MCI's general attack on the Commission's allocation of access charges between carriers and private line users is ill-founded. The Communications Act prohibits unjustifiably different rates for the same service. 47 U.S.C. § 202(a) (1976). But when there is a neutral, rational basis underlying apparently disparate charges, the rates need not be unlawful. For instance, when charges are grounded in relative use, a single rate can produce a wide variety of charges for a single service, depending on the amount of the service used. Yet there is no discrimination among customers, since each pays equally according to the volume of service used.

This is the neutral, reasonable principle underlying the disparities in per line access rates charged to OCCs and private line users. Although OCC's will pay many more dollars per line for access charges, they require and use a correspondingly higher volume of exchange access on each line. Between OCCs and leaky PBX users the size of the per line access charges has a definite relation to the volume of access minutes attributable to each line. There is essentially no difference in the per minute rate charged to either class of access users.

Slight variations in rates identified by MCI are generally attributable (1) to the Commission's decision to compute the individual line charges based on the class-wide volume of access, or (2) to the difficulty of measuring the precise number of access minutes used by the PBX-private line subscribers. These choices are rationally necessary to minimize difficulties in administering the access charges and are within the range of the Commission's discretion. *See infra* B.1.c., B.2. The resulting rates do not rise to the level of "unjust or unreasonable" discrimination. 47 U.S.C. § 202(a) (1976).

The Commission held that the previous potpourri of access compensation arrangements was unlawful because there was no "reasonable or rational relationship to justify the wide disparities in charges." *Access Order* ¶ 51, 93 F.C.C.2d at 258. The different rates could not be explained on the basis of functional differences in the type of access service offered, variations in the cost of providing that service, or the dissimilar amounts of access usage. *Id.* Correction of the illegality could be accomplished through the imposition of a single, neutral principle, such as relative use, without necessarily equalizing the amount paid by each access user for exchange access.

The Commission's decision to recover NTS access costs from carriers on a usage sensitive basis is not inherently discriminatory. *Cf. MCI Telecommunications Corp. v. FCC*, 675 F.2d 408, 414-16 (D.C. Cir. 1982). Usage-based rates have long been imposed in the telecommunications industry. *See, e.g., In re: AT&T*, 9 F.C.C.2d 30, 93 (1967). Under the prior system most NTS costs were recovered through usage-based toll charges levied by AT&T for long distance telephone traffic, but different classes of carriers and private line users paid unequal rates. Now that the rates for each minute of exchange access have been equalized on an average basis there is no justification for a holding that the continuation of

usage-based rates perpetuates the previous discrimination found to exist.

Although the Commission's decision can be explained based on relative use, MCI claims that the circumstances of this proceeding make the Commission's choice unreasonable, and therefore unlawful. MCI and other petitioners also contend that the plan unlawfully discriminates among the various classes of carriers and private users on factors extraneous to usage. We consider each of these objections in turn.

c. The Reasonableness of Adopting Usage-Based Charges for Carriers and Private Line Users Requiring Exchange Access

MCI contends that the Commission's decision to recover NTS costs through usage sensitive carrier charges is unlawful on several grounds. First, the Commission itself determined that NTS costs, which by definition do not vary with usage, should in principle be recovered on a flat-rate basis from end users; its departure from that principle without adequate explanation is assertedly arbitrary and capricious. MCI also argues that a usage-based plan could not properly be chosen to avoid extreme rate increases which could have caused disruptive service impacts. Finally, MCI contends that the plan would be unreasonably difficult to administer and should therefore not have been adopted.

These claims are not frivolous, *Telocator Network of Am. v. FCC*, 691 F.2d 525, 537 (D.C. Cir. 1982), but inevitably misconstrue the breadth of the Commission's statutory discretion to balance the multiple goals embodied in the Communications Act. They may suggest that the Commission could have reasonably elected to implement a nonusage based scheme for recovering exchange access costs from carriers and other private line users, but they hardly prove error in choosing a usage-based recovery plan.

Recovery of the balance of NTS costs through the usage-based carrier common line charge and special access surcharge is not inconsistent with the decision to impose flat-rate end user charges. The Commission reasonably determined that NTS exchange costs are caused by subscribers, and should economically be recovered from the customers incurring those costs. *Reconsideration Order* ¶ 10, 48 Fed. Reg. at 42,987. The portion of costs which temporarily or permanently will not be borne by the end users, which forms the basis for carriers' access charges, is essentially a subsidy. This subsidy is not logically attributable to a particular class of carriers. The Commission's decision to recover NTS costs from end users on a flat-rate basis therefore does not require it also to assess the subsidized balance of those costs on a flat-rate basis from the interexchange carriers.

Moreover, the Commission carefully considered allegations that its usage-based recovery scheme was inconsistent with the general decision to promote economic efficiency by imposing flat rates to recover NTS costs:

> Several petitioners seek . . . complete elimination of the [carrier usage charge]. SBS argues that the charge is inefficient since it is not cost-based . . . .
>
> [These petitioners] are legitimately concerned about the possible uneconomic effects of the Carrier Common Line charge. Such charges do reduce the relationship between rates and costs causation. Nevertheless, as the *Access Charge Order* stresses, for the most part the Carrier Common Line charge is a transitional charge. We explicitly recognized the economic costs of such a charge but viewed these costs as acceptable consequences of a gradual and certain transition. None of the petitions were able to suggest any alternative mechanism to produce such a transition. We, therefore, reject any sugges-

tion that the carrier usage or Carrier Common Line charge be abandoned.

Id. ¶¶ 65-66, 48 Fed. Reg. at 42,994 (footnotes omitted). Other aspects of the Commission's orders make it reasonably clear that a *usage*-based transition plan would help avoid disruptions in private line usage and other burgeoning interexchange telecommunications services which would have contradicted the very goals of a measured transition. *Id.* ¶¶ 77, 83, 90, 48 Fed. Reg. at 42,995-96, 43,000. Harsh results would have attended adoption of a flat-rate carriers' charge such as that now proposed by MCI. That risk was evident even under the usage-based recovery plan adopted by the Commission, *see id.*; it would likely have been magnified under a flat-rate approach.

The choice of a usage-based scheme for the largely transitional carrier common line charge and private line surcharge was properly influenced by the need to avoid the disruptions in service which could have accompanied a flat-rate carriers' charge. Our conclusion today that the Commission may lawfully impose flat-rate end user access charges on a gradual basis in order to preserve universal service is premised on the holding that rates may be structured to avoid disruptive service impacts. When necessary to avoid excessively burdening carriers, the gradual implementation of new rates and policies is a standard tool of the Commission. *E.g.*, *Uniform System of Accounts*, 85 F.C.C. 2d 818, 828 (1981); *ENFIA*, 71 F.C.C. 2d 440, 455 (1979). *See also National Association of Independent Tel. Producers & Distributors v. FCC*, 502 F.2d 249, 253-55 (D.C. Cir. 1974). The Communications Act authorizes the Commission to impose reasonable charges to promote a rapid, efficient, and modern telecommunications network in which technological innovations are encouraged in order to permit the development of facilities adequate to provide this service. *See* 47 U.S.C. § 151 (1976). MCI has itself benefitted from transitional rate structures implemented to avoid poten-

tially fatal rate increases both under the ENFIA agreement [34] and under the Commission's access charge scheme, in which OCCs pay a lesser rate for their access connections than does AT&T although the equivalent costs of providing that OCC and AT&T access may not be fully reflected in the rate differential.[35] The shift from one type of nondiscriminatory rate structure to another may certainly be accomplished gradually to permit the affected carriers, subscribers and state regulators to adjust to the new pricing system, thus preserving the efficient opera-

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[34] Under the ENFIA agreement, OCCs paid progressively higher access rates. That transitional scheme was based partially on the increasing quality of interconnection, but also reflected a compromise rate level between the access rates paid by AT&T under separations regulations and that paid by other customers for local access. *See* ENFIA, 71 F.C.C. 2d 440, 446-47, 455 (1979); ENFIA, 90 F.C.C. 2d 6, 16-17 (1982). The OCC rate effectively increased as the volume of OCC business also increased, even though the quality of access was not correspondingly higher. *See* Brief for FCC at 78.

[35] The Commission stated that while the physical facilities used to promote exchange access to OCCs may provide a lower quality interconnection than that offered AT&T, "[i]t is not clear, however, that this inferior level of interconnection is any cheaper to provide. Cost-based pricing would appear to require that all carriers pay their full costs regardless of any quality differences." *Access Order* ¶ 151, 93 F.C.C.2d at 286. By determining that OCCs should not be required to pay the higher effective access rates levied against AT&T the Commission expressly acted to ameliorate the adverse impact on the OCCs' customer base which would have accompanied fully equivalent rates for varying quality access costing roughly the same to provide. Those aspects of the Commission's orders charging different access rates to AT&T and MCI are under appeal in a separate proceeding, AT&T v. FCC, No. 84-1087 (D.C. Cir. filed March 9, 1984). We express no opinion on the issues raised in that proceeding, holding only that transitional considerations based on preserving universal subscription and avoiding disruptions in service may lawfully be considered in structuring a rate scheme.

tion of the interstate telephone network during the interim.

Other claims have been made that a usage-based access charge plan would be unreasonably difficult to administer. Those arguments generally revolve around the difficulty of accurately measuring the relative use, or the problems associated with distinguishing between classes of carriers, such as resellers and sharers. However, it is apparent from our review of the record that the Commission thoroughly reviewed these problems and made a reasonable determination that other alternatives posed even graver risks to its articulated goals. *See National Indus. Sand Ass'n v. Marshall*, 601 F.2d 689, 699-700 (3d Cir. 1979).

Moreover, the Commission made every attempt to mitigate these perceived problems. It made the most precise measurements of average relative use possible. It expects that carriers will devise even more accurate methods of determining PBX leakage, and will revise the measurements when that becomes possible. The Commission identified means of distinguishing between resellers and other classes of exchange users, and cautioned that the difficulty of drawing those lines should not become a pretext for discrimination. *Reconsideration Order* ¶ 84 n.61, 48 Fed. Reg. at 42,997. It recognized that although "certain resellers canot be identified, . . . the surcharge which applies to private lines will apply to them as well, and will similarly serve as a temporary surrogate for interstate access charges." *Id.* ¶ 84. No party proposed a coherent, feasible alternative scheme which would have better served the diverse and delicately balanced goals identified by the Commission.

We have certainly been unable to divine the existence of such an alternative plan; and we fail to see how a remand for further reconsideration could possibly improve on the Commission's thorough assessment of these issues. The FCC's choice of a usage-based system of car-

rier common line charges and private line surcharges is reasonable under the circumstances.

d. Discrimination in the Uniform Access Compensation Plan

Several parties allege that the Commission implemented its plan for carriers access charges in an illegally discriminatory manner. The primary claim appears to be that the Commission impermissibly discriminated against OCCs and resellers in favor of the closely related enhanced service providers and some sharers. Although the latter carriers may, at times, heavily use exchange access, they are subjected only to the lesser private line surcharge. The access charges paid by the sharers and enhanced service providers may thus not fully reflect their relative use of exchange access.

To analyze the lawfulness of that classification, we begin with the language of the Communications Act:

> It shall be unlawful for any common carrier to make any *unjust or unreasonable* discrimination . . . for . . . like communications service, . . . or to make or give any *undue or unreasonable* preference or advantage to any particular person, . . . or to subject any particular person, . . . to any *undue or unreasonable* prejudice or disadvantage.

47 U.S.C. § 202(a) (1976) (emphasis added).

The Communications Act thus does not prevent all discrimination—disparities in prices for similar service—but only *unreasonable* discrimination. *Associated Press v. FCC*, 452 F.2d 1290, 1300, 1301 (D.C. Cir. 1971). The reasonableness of the price disparity must be judged by the circumstances in which it is assessed.

The Commission justified its decision to impose the private line surcharge on enhanced service providers and sharers as necessary to preserve their financial viability, and hence avoid adverse customer impacts. *Reconsideration Order* ¶ 83, 48 Fed. Reg. at 42,997. That conclu-

sion represents its considered judgment that the benefits to be achieved through preservation of an efficient telecommunications network are more important than adhering to an inflexible access charge plan. It is difficult to quarrel with this judgment, since the Commission anticipated that the general level of access fees may fall as the usage-based system of charges is perfected. Another plan could unnecessarily pretermit the existence of these valuable telecommunications services.

Moreover, this plan merely extends to the enhanced service providers and some sharers the benefits of a graduated transition which was previously granted to those carriers subject to ENFIA tariffs. These carriers were not generally regulated under ENFIA and the Commission recognized that they had not yet had time to adjust their business operations to compensate for higher access charges. *Id.*

On balance, the Commission's decision to avoid unnecessary "customer impact or market displacement" reasonably justifies any slight rate disparities implemented under the new access charge plan. *Id.* Neither the Commission's rulings [36] nor our cases have ever held that all pricing disparities which may fail to recover full costs from the customer—however temporary or necessary to achieve the statutory policies of the Communications Act—are invariably banned by the antidiscrimination sections of the Act.[37] The Commission thus warned in its

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[36] *E.g., Access Order* ¶ 33, 93 F.C.C.2d at 252: "[T]his decision [to address the problem of uneconomic bypass] does not, in any way, constitute a judgment that subsidizing the costs of basic telephone service for certain customers or for all customers is improper." *See also* AT&T, 78 F.C.C. 2d 1296, 1297 (1980). Of course, the Commission's finding of an unjustified subsidy may precede a holding that rates are unreasonably discriminatory. *See, e.g.,* Western Union Int'l, Inc. v. FCC, 568 F.2d 1012, 1019 (2d Cir. 1977).

[37] American Trucking Ass'ns, Inc. v. FCC, 377 F.2d 121, 129-31 (D.C. Cir. 1966), *cert. denied,* 386 U.S. 943 (1967),

initial order that it would be impossible to implement a perfect plan:

> An ideal access charge plan would eliminate all discrimination or preferences within or among services, create incentives for the most efficient utilization of all telecommunications facilities, discourage all uneconomic bypass, ensure that no local exchange service subscriber cancels that service, and establish full and fair competition in the interexchange services market. All of those objectives could not be fully accomplished simultaneously and immediately even if we had perfect knowledge. Therefore, we necessarily must exercise judgment and discretion in devising an access charge plan that takes all of those objectives into account.
>
> Neither the language of the Act nor past court or Commission opinions preclude this Commission from striking a reasonable balance. On the contrary, Congress undoubtedly anticipated that an exercise of judgment would be required when it declared that it was creating this Commission in order to achieve multiple purposes "so far as possible."

Access Order ¶¶ 88-89, 93 F.C.C. 2d at 268.

In requiring the enhanced service providers and sharers to pay the private line surcharge rather than the carrier common line charge the Commission acted to end existing discrimination as far as possible. We uphold its choice under these circumstances.

Resellers also object to their treatment under the Commission's plan. However, they have generally been pay-

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establishes only that *once the Commission has identified a rate as unlawfully discriminatory*, the carrier is not entitled to perpetuate that rate as serving other important policy interests under the Act. *Cf.* Aeronautical Radio, Inc. v. FCC, 642 F.2d 1221, 1237 (D.C. Cir. 1980), *cert. denied*, 451 U.S. 920 (1981) (Wilkey, J., dissenting); Nader v. FCC, 520 F.2d 182, 211 (D.C. Cir. 1975) (Fahy, S.J., dissenting) (both cases upholding FCC action in the absence of an initial finding of unlawful discrimination).

ing ENFIA rates and have thus had the benefit of a gradual transition. When offering resale of long-distance services they use the local exchange facilities in a similar manner and amount as OCCs. *See* Brief for FCC at 79 n.103; *AT&T—Applicability of the ENFIA Tariff to Certain OCC Services*, 91 F.C.C. 2d 568, 569, 575-77 (1982), *aff'd mem.*, *U.S. Telephone Communications, Inc. v. FCC*, No. 82-2324 (D.C. Cir. Jan. 13, 1984). The Commission rationally held that carriers reselling private line services to provide long distance service are situated similarly to OCCs, and should thus be subject to the carrier common line charge.

MCI asserts that the Commission unlawfully discriminated by not requiring exchange carriers to file tariffs for privately owned telecommunications systems, although these systems are capable of accessing the local exchange. Brief for Petitioner MCI at 69. However, the Commission did permit carriers to file tariffs. Its decision not to make filing mandatory is reasonable since it is not yet clear whether exchange carriers have the measurement and other technical capabilities to develop a surrogate surcharge which could sufficiently approximate usage and satisfy the statutory limits on traiffs. *See Further Reconsideration Order* ¶ 133, 49 Fed. Reg. at 7826. Agency action which fails to require that exchange carriers perform the impossible is hardly unlawful.

We have thoroughly considered the parties' remaining claims of discrimination, which, although numerous, are without any substance; these appear to be set out as hollow decoys to distract attention from the expert manner in which the Commission thoroughly balanced the complex, often contradictory, policies of the Communications Act. The Commission has, to the best of its ability, attempted to reconcile existing disparities in charges levied against interexchange carriers and private line users. Its plan to recover specified access costs through a combination of usage-based carrier common line charges

and private line surcharges is appropriately tailored to minimize the difficulties inherent in any transition to a new system of rates; it is designed to guarantee the widest possible participation among all classes of exchange access users; and it is neutrally imposed on the basis of relative use. Certainly, therefore, this plan falls within the broad zone of expertise and discretion which must be granted to the Commission in a proceeding which touches the very core of the rapidly developing telecommunications industry.

2. *Private Line Service*

We next turn to consider the FCC's action with regard to private line/PBX service ("PBX"). The Commission recognized in its *Second Supplemental Notice* that these communications services posed special problems for any new regulatory regime that sought to move the industry to a more efficient, cost-based footing.[38] These problems were rooted in the fact that the large portion of PBX users possessed the capability to circumvent the conventional long-distance network and yet achieve interstate connections beyond those envisioned by the private line service. These connections—their frequency and duration—are not measured, nor will they be, at least in the short-term future. Thus PBX use posed a classic "free-rider" dilemma: PBX users enjoy the benefits of non-traffic sensitive equipment, but do not contribute to the cost of maintaining the interstate equipment.

The FCC has determined that some of the costs associated with such "leaky" PBX use must be recovered. To this end the Commission devised a surcharge:

> [T]he most reasonable interim approach to reducing the discrimination in rates for MTS [long

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[38] *MTS & WATS Market Structure, Report and Second Supplemental Notice of Inquiry,* 77 F.C.C.2d 224 (1980) ("*Second Supplemental Notice*").

distance] users and . . . other persons would be to develop a surcharge on private lines and the closed ends of WATS lines. We determined that a surcharge would be imposed on the closed ends of all interstate WATS lines as well as all jurisdictionally interstate private lines not falling within specifically enumerated exceptions. These exceptions included: (1) private lines subject to carrier's carrier charges; (2) private lines that cannot leak; and (3) certain private lines that can but probably do not leak (*i.e.*, Telex and programming facilities). We established a flat surcharge of $25 per voice grade line for 1984 only because insufficient time remained for the telephone companies to develop a system of surcharges more precisely reflecting actual leakage before the October 3 deadline for filing access service tariffs. *See Reconsideration Order* at para. 88. We expressed our expectation that telephone companies would act to replace the $25 surcharge by such a system of surcharges as soon as possible.

Further Reconsideration Order, ¶ 112, 49 Fed. Reg. at 7824. The Commission explained that this surcharge concept was the best alternative open to it: "The imposition of a modest surcharge that is not based upon actual usage measurements will reduce discrimination or preferences to the maximum extent possible without imposing costly and difficult measurement procedures." *Id.*, ¶ 116, 49 Fed. Reg. at 7824. The choices open to it were few, the Commission explained, and it described the difficulties attendant to each possible course. *Id.*, ¶¶ 117-119, 49 Fed. Reg. at 7825. It is a remarkably candid review of the options open to the Commission. The computation by which the $25 per line figure was arrived at is contained in paragraph 88 of the *Reconsideration Order*.[39] It is by

[39] "[W]e shall use our best judgment to develop an initial surcharge level, pending development of [other] charges by the carriers. First, we note that private lines attached to a PBX are capable of 'leaking' into local exchange. Because most private lines are connected to PBXs, most private lines are

admission an estimate based upon assumptions drawn from the collective experience of the Commission. It appears to be a conservative estimate. It evidences the Commission's judgment based upon the agency's expertise and experience collected over a great many years. It also represents, we conclude, an example of exactly the kind of difficult judgment call for which expert agencies have been created.

As is to be expected with any decision that departs from the status quo, the beneficiaries of the status quo have objected to the Commission's plan. Aeronautical Radio, Inc. ("ARINC"), a heavy subscriber to private line service, summarized its objections to the $25 charge this way:

> The Commission . . . erred in prescribing a special access surcharge to be imposed upon the terminations of private lines which bears no relationship either to the amount of usage alleged [to] be made of the local exchange by such lines or the cost there-

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capable of leaking. Although one might assume that all private lines would leak if capable of doing so, we are aware of some private lines connected to PBXs that actually may not be used in connection with local exchange services to make interstate calls. We believe a fair estimate of the number of such lines would be 20 percent of all private lines. Thus, we estimate that 80 percent of all private lines do leak through a PBX or other patching or switching device. We shall assume that 8 percent of all communications made over such lines are interstate, based on the latest data available to us on average subscribed line usage for interstate MTS and WATS services. Eight percent of 80 percent is 6.4 percent, which represents the proportion of all private line usage that "leaks" into the local exchange. We further assume, based on estimates submitted in this proceeding, that nonpremium carriers would pay approximately $400-$500 in monthly carrier usage charge under the access charge plan. Taking 6.4 percent of these figures, we arrive at a range of approximately $25-$32 per month per line. We will select the lower end of this range, $25, as a conservative estimate of what the interim surcharge should be." *Reconsideration Order*, ¶ 88, 48 Fed. Reg. at 42,999.

> by imposed upon the exchange. In attempting to develop a value for the surcharge, the FCC relied upon unsupported and facially unreliable estimates of interstate private line usage which, in any event, are wholly irrelevant to the amount of private line traffic which might "leak" into the local exchange through private switching arrangements. The Commission's manifest failure to articulate a rational basis for its determination of the special access surcharge, and its admitted reliance upon unrelated and irrelevant data in determining the value of that charge, clearly requires remand to the agency.

Brief for ARINC at 30.

The FCC responds by noting that "[n]o data are presently available on the percentage of private lines that are connected to PBXs or other switching machines. . . . Because private lines are not routinely metered, the FCC also had no data on the extent of 'leakage' from such private lines or on the percentage of leakage that is jurisdictionally interstate. . . . Rather than abandon entirely the possibility of recovering a fair part of interstate local exchange costs from private line users, the FCC undertook to develop a reasonable surrogate for the carrier charges." Brief for the FCC at 97-98. The Commission adds that "[n]o one seriously challenges the more general proposition that private lines generate extensive traffic for local exchanges; and none of these who challenge the 80 percent figure offers a different estimate." *Id.* at 98 & n.130. AT&T adds in support of the Commission action that "[o]nce the use of NTS plant by special access line users is recognized, the only remaining question is the amount the user should contribute." Brief for AT&T at 49.

In our judgment both the concept of a surcharge and the rate are lawful exercise of the statutory discretion vested in the FCC. The objections thereto are founded on faulty premises regarding the role of this court. We are not a policy-making body. This court instead patrols the perimeters of an agency's discretion. If an agency in the

course of an informal rulemaking does not attempt either to close itself off from informed opinion or to extend its reach beyond the scope of permissible authority, then it is our duty to accept that judgment if it is rational and not unreasonable. The fact that an agency's decision is a difficult one, or that the decision rests on a set of evidentiary facts less desirable or complete than one which would exist in some regulatory utopia does not alter our role. We remain here to insist upon a necessary minimum: "[When an agency] is obliged to make policy judgments where no factual certainties exist or where facts alone do not provide the answer, [it] should so state and go on to identify the considerations [it] found persuasive." *Industrial Union Department, AFL-CIO v. Hodgson*, 499 F.2d 467, 476 (D.C.Cir. 1974). We cannot here conclude that "the FCC failed to take a sufficiently careful look at the problem presented, and failed to engage in reasoned decision making with respect to the issue . . . ." *Aeronautical Radio, Inc. v. FCC*, 642 F.2d 1221, 1231 (D.C.Cir. 1980), *cert. denied*, 451 U.S. 920 (1981). The agency has not given us "[p]ious hope and speculation [in the place] of evidence." *Natural Resources Defense Council, Inc. v. EPA*, 655 F.2d 318, 346 (D.C.Cir.) (Robb, J., dissenting), *cert. denied*, 454 U.S. 1017 (1981). Rather, it appears from the record that the FCC has spent considerable time and resources in dealing with the PBX problem, and it has indicated that it will continue the search for a better resolution. "[T]he Commission must be expected to make use of the experience it has gained through years of dealing with the problem. . . ." *City of Chicago, Illinois v. Federal Power Commission*, 458 F.2d 731, 747 (D.C.Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972). "[E]ffective regulation requires that the Commission bring to bear the full range of its knowledge, garnered from whatever source, in making the interpretation on which it bases important policy decisions." *Id.*

The critical choice confronting the agency was either to do nothing about the "hidden" access enjoyed by PBX

users, or to do something. The fact that PBX users could and do use the local networks dictated that the FCC seek some form of cost contribution. Such was not only a rational decision, it is in fact the only decision that is rational given the broader context of the FCC's plan for the nation's communication system.

Given this choice, the next critical question was how to cope with a problem about which no reliable data was available. The FCC chose to rely upon its historical experience and expertise to employ a system of conservative estimates. As discussed *supra*, some parties have assailed this choice because of their belief that it demands of free riders only a minimal fare. ARINC and others criticize the decision for demanding too much. We view it as one of a number of choices, any one of which would have been within the agency's broad discretion. When "the figure selected by the agency reflects its informed discretion, and is neither patently unreasonable nor 'a dictate of unbridled whim,' then the agency's decision adequately satisfies the standard of review." *WJG Telephone Co., Inc., v. FCC*, 675 F.2d 386, 389 (D.C.Cir. 1982). We note also that this rate is not one for the ages. It is an interim charge, imposed because of necessity. "The $25 surcharge applies only in 1984, 47 C.F.R. § 69.115(c), and the FCC said that it would reassess the level of the surcharge after 1984 in a separate proceeding." Brief for the FCC at 100, n.135.

The great part of the attack on the surcharge centers on the method the FCC employed in arriving at the $25 figure. *See* Brief for ARINC at 43-45; Brief for API at 32-34. ARINC and others would prefer that this court's focus be confined to the particulars of this calculation and not the broad contours of the dilemma facing the Commission. It did not furnish the Commission, and it does not furnish the court, with any alternate methodology, much less one that is a persuasive substitute. Each step in the FCC's calculation is to some extent guesswork, but it is *reasoned* guesswork. It is plausible. It is tethered to the Commission's general experience with long-distance use.

We remind ARINC that "some legislative judgments cannot be anchored securely and solely in demonstrable fact." *Industrial Union Department v. Hodgson, supra,* 499 F.2d at 476. Of course we would prefer a more precise equation. But "[s]ound principle bids us accompany any further judicial review—of the specifics of these approaches and tracing methodologies—with diffidence and restraint." *National Association of Greeting Card Publishers v. United States Postal Service,* 607 F.2d 392, 401 (D.C.Cir. 1979), *cert. denied,* 444 U.S. 1025 (1980). "The thoroughness and persuasiveness of the explanation we can expect from the agency will, of course, vary with the nature of the prediction undertaken." *Natural Resources Defense Council, Inc. v. EPA, supra,* 655 F.2d at 329. Here the prediction is one concerning the amount of use made of PBX facilities to connect with local loops. We cannot say that the prediction is unreasonable or unsound. The Commission "must be free, within the limitations imposed by pertinent constitutional and statutory commands, to devise methods of regulation capable of equitably reconciling diverse and conflicting interests. . . ." *Permian Basin Area Rate Cases,* 390 U.S. 747, 767 (1968).

ARINC argues that the FCC has not met its obligation to justify its policy choice, that the agency has somehow failed to carry its burden of proof in establishing the $25 figure. This is not a novel tactic. Nor is our response original: "Without embarking upon an extended discussion of burdens of proof, we think this view is manifestly unsound." *Telocator Network of America v. FCC,* 691 F.2d 525, 539, n.114 (D.C.Cir. 1982). It is not the Commission's chore to convince us that what it has done is the best that could be done, but that what it has done is reasonable under difficult circumstances. Here the unique nature of an unmeasurable but real problem of hidden access assists the FCC in justifying what it has ordered.

We cannot divorce the difficulty of the regulatory dilemma from the reasonableness of its resolution. The

manifest equity of demanding some contribution to the upkeep of the system from PBX users combined with the current impossibility of more precision renders our conclusion unavoidable. Repetition of the phrase "arbitrary and capricious" may have dulled it and left less than obvious its primary meaning. But when an agency makes rational choices from among alternatives all of which are to some extent infirm because of a lack of concrete data, and has gone to great lengths to assemble the available facts, reveal its own doubts, refine its approach, and reach a temporary conclusion, it has not acted arbitrarily or capriciously. "The Commission, as the expert agency entrusted by Congress with the administration of the crucial, dynamic communications field, requires and deserves some latitude in carrying out its substantial responsibilities." *Action for Children's Television v. FCC*, 564 F.2d 458, 482 (D.C.Cir. 1977). We thus conclude that the $25 rate was validly imposed.

3. *Private Communications Systems*

Clearly connected to the discussion of private line/PBX service is that small portion of the Commission's order concerning private, not-for-hire communications systems. Regarding these systems the Commission commented:

> [W]e shall allow exchange carriers to develop reasonable, nondiscriminatory surcharges on interconnected use of exchange services by carriers' publicly offered interstate services using radio and other facilities (e.g. DTS), and privately-owned microwave relay systems, satellite transmission systems, and other interstate private facilities that would otherwise not be subject to either the surcharge or carriers access charges (that is, that will not employ any end links obtained from the exchange carriers to which private line surcharges would apply). In such cases, we are prepared to consider the carriers' proposals for a surcharge to the individual exchange

> telephone lines which can be connected to such systems. Such a surcharge would have to be filed in tariffs with this Commission.

Reconsideration Order, ¶ 86, 48 Fed. Reg. at 42,998. The Commission was obviously concerned with the possibility that private communications systems, such as satellite transmission systems, might be enjoying or might soon enjoy the kind of hidden access to the nation's telephone network which the PBX users currently possess. It thus acted to open the floor to proposals, in the form of carrier-proposed tariffs, on how to assess the costs of such access. Predictably, the users or potential users of in-place or projected systems reacted as though possible future levies had already been laid and collected.

Intervenors American Petroleum Institute, the Association of Data Communications Users, and the Utilities Telecommunications Council (hereinafter referred to collectively as "API") argue that:

> Those provisions [of the FCC's order] which authorize telephone companies to file the surcharges on private communications systems in federal access tariffs were issued without notice and opportunity for comment. Not once during the five-year history of this rulemaking proceeding has the Commission provided notice that it intended to impose surcharges upon private communications systems that engage local exchange facilities.

Brief for API at 17-18.

The FCC responds by raising three arguments: 1) that API is barred from seeking court review of its arguments because it failed to seek agency reconsideration of the issue; 2) that parties in API's position "should have been aware that the Commission might consider" access charges for those systems, and 3) "[i]n any event, the Commission took no action with respect to private systems that could be considered a 'rule' . . . and thus the notice and comment requirements . . . were not triggered."

Brief for FCC at 117. API has failed to raise any issue here that could be considered ripe for review.

The basic components of the ripeness doctrine were laid out by the Supreme Court nearly two decades ago in *Abbott Laboratories v. Gardner*, 387 U.S. 136 (1967), when the court stated:

> Without undertaking to survey the intricacies of the ripeness doctrine it is fair to say that its basic rationale is to prevent the courts, through avoidance of premature adjudication, from entangling themselves in abstract disagreements over administrative policies, and also to protect the agencies from judicial interference until an administrative decision has been formalized and its effects felt in a concrete way by the challenging parties. The problem is best seen in a twofold aspect, requiring us to evaluate both the fitness of the issues for judicial decision and the hardship to the parties of withholding court consideration.

Id. at 148-149. While ripeness questions frequently recur, this formulation of a court's inquiry remains the guide to any particular controversy. *See Baltimore Gas and Electric Company v. ICC*, 672 F.2d 146 (D.C.Cir. 1982). Applied here it is easy to see that the issues pressed by API are not currently fit for review, nor does API yet bear any burden as a result of the Commission's announcement.[40]

What the FCC has done is to serve notice that it considers the hidden access—if any—enjoyed by private communications systems to be a subject worth studying

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[40] API's counsel stated at argument that his clients would be forced to deal with multiple state commission filings as a result of the Commission's statement. We do not view such efforts as the kind of "burden" envisioned by the *Abbott* test. Interested parties will of course have to maintain surveillance of the regulatory environment in which they function. But this is an ordinary cost of doing business, and is not an inescapable result of the Commission's announcement.

and possibly a problem requiring a remedy. It has invited the exchange carriers to conduct such studies and, if warranted, to propose a method of cost recoupment for any hidden access that is discovered to exist. The invitation is not, as we read it, an exclusive one. Subscribers to private systems would no doubt be well-advised to assist the exchange carriers in their assessment of the problem. Nor does the wording of the announcement preclude an extended and in-depth agency consideration of any proposals if and when they should materialize. But the agency has as yet decreed nothing, and parties such as API are as yet paying nothing. Likewise, we have nothing concrete to review.

We emphasize that the agency's announcement and our comments on it in no way preclude or in any way limit the right of a user of a private system to later challenge the lawfulness of any charges developed by the exchange carriers. We remind the Commission that the agency cannot limit any future proceeding in this area by reference to its decisions in this docket. We also caution the Commission that it cannot, of course, cede to private parties such as the exchange carriers either the right to decide contests between themselves and their opponents or even the opportunity to narrow the margins of the debate regarding access charges for private systems. API seriously contends that the Commission is unlawfully delegating agency authority. *See* Brief for API at 42, n.40, *citing Sierra Club v. Sigler*, 695 F.2d 957, 963, n.3 (5th Cir. 1983). Such argument is typically presented in the context of a transfer of legislative authority from the Congress to agencies, but the difficulties sparked by such allocations are even more prevalent in the context of agency delegations to private individuals.[41]

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[41] Recent years have witnessed a renewal of interest in the traditional role of nondelegation doctrine. *See* American Textile Mfgs. Inst., Inc. v. Donovan, 452 U.S. 490, 543-48 (Rehnquist, J., dissenting). *See also*, Note, "Rethinking

We need not examine the problem because we divine no such abdication of the Commission's role as disinterested arbiter to any interested party. Had the Commission so acted and had the Congress so intended it to act, that would amount to a "legislative delegation in its most obnoxious form; for it is not even delegation to an official or an official body, presumptively disinterested, but to private persons whose interests may be and often are adverse to the interests of others in the same business." *Carter v. Carter Coal Co.*, 298 U.S. 238, 311 (1936). Since the FCC has here retained its final authority over these possible surcharges, which cannot go into effect unless and until the Commission approves them, and since the Commission has not prescribed any formula for their composition, it is premature to accuse the agency of an unlawful delegation. Nor will it be open to the charge if, upon presentment by any exchange carrier of its plan for imposing such charges on private system in the future, it takes due note and careful consideration of the views of all interested parties. For the present, however, there is no case that presents any issue that is ripe for review.

4. *Foreign Exchange ("FX") Service*

Foreign exchange ("FX") service is another component of the nation's communication system.[42] "Foreign exchange service is a combination of a local telephone access with a

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the Nondelegation Doctrine", 62 B.U.L.Rev. 257 (1982), Lane, "*Schechter* and the FTC: A Roving Commission", 39 Bus. Lawyer 153 (1983). As attention to this area of our law grows, it refocuses thought on one of the rationales against excessive delegation: the harm done thereby to principles of political accountability. Such harm is doubled in degree in the context of a transfer of authority from Congress to an agency and then from agency to private individuals. The vitality of challenges to the former type of transfer is suspect, but to the latter, unquestionable.

[42] "Foreign" indicates an exchange in another state, and not one in a foreign country.

dedicated intercity private line which permits the public to call a local number to reach an . . . office in a distant city." Brief for ARINC at 6, n.3. "For example, if an airline with a central reservation office in Kansas City acquires FX service between Kansas City and Denver, a potential Denver customer can dial a 7-digit local phone number in Denver—the 'open end'—to reach the Kansas City reservation bureau—the 'closed end'." Brief for the BOCs at 66, n.75. Every call going out through an FX number is an interexchange long-distance call. Thus every FX call uses the local loop's non-traffic sensitive equipment. This is undisputed. Under the old regime, however, FX users paid only the cost of a local business line and made no contribution for access to the "foreign exchange" similar to that assessed users of MTS/WATS or equivalent OCC-provided long distance services. FX users enjoyed a uniquely privileged spot in the rate structure.

The FCC determined that this special preference within the rate structure had to be eliminated. The Commission commented in its *Access Order* that

> [T]he current methods of recovering costs of jointly used non-traffic sensitive subscribed plant for MTS, open-end FX, CCSA and WATS service and the ENFIA services are totally different and produce widely differing results even though each service uses the same plant in the same manner. The FX and CCSA services pay local exchange rates for open end access, the MTS/WATS equivalent services must pay the higher ENFIA rates, and MTS and WATS pay even higher access compensation through the settlements and divisions of revenue process.

Access Order, 93 F.C.C.2d at 258. As discussed, *supra*, the FCC, as one of its ultimate goals, projected a single-tier rate structure within which all providers of interstate service would pay the same carrier access charges. As a way station on the road to equal rates, however, the FCC established a two-tier system that recognized the reality

of premium access enjoyed by some carriers, primarily AT&T. The OCCs thus will temporarily pay less in recognition of their inferior access. The FCC also chose to place the FX users into this second tier and, recognizing that while most FX users depend heavily upon the service, others use it only lightly, the Commission also determined that carriers would recoup the cost of access on a minutes-of-use basis rather than through a flat charge.

While ARINC initially applauded the FCC's proposal to move the industry to a cost-based footing for access, *See* Comments of Aeronautical Radio, Inc. at J.A. 1387, its enthusiasm quickly waned when it became apparent that the new plan would require of FX users that which it would require of all other equivalent services—payment of a fair share of their attributable costs. *See* Opposition of ARINC at J.A. 2469. ARINC's stake in the treatment of FX service is considerable:

> The airlines have established a system of some 12,000 foreign exchange ("FX") circuits to provide the public with toll-free access to airline information services. Use of FX lines enables the airlines to absorb the cost of intercity calls when members of the public contact an airline office in a distant city for flight information, reservations, and other services.

Brief for ARINC at 6. The FCC's plan presented the airlines with an "increase from a typical $30 per month charge for business service at FX open ends to, as a minimum, the $235-plus per month non-premium carrier charge, *some eightfold increase*." *Id.* at 32 (emphasis in original). ARINC's most recent estimate of the total cost increase the airlines will incur is approximately $30 million annually. Reply Brief for ARINC at 18, n.20. We have no reason to doubt the accuracy of ARINC's cost forecasts.

The FCC's response to ARINC's complaints appeared first in its *Further Reconsideration Order*. The Commission noted that "FX customers pay substantially less for each minute of use of the foreign exchange's local

network than would an MTS customer or the customer of an OCC using that carrier's MTS-like service." *Id.*, ¶ 99, n.46, 49 Fed. Reg. at 7822. The FCC then responded to ARINC's comments:

> The ARINC petition apparently requests that initial access charges for open end FX access be established at a level that is lower than the access charges for MTS/WATS equivalent services in order to provide FX users with a more gradual transition from the existing charges. . . . The rules that we adopted in the *Access Charge Order* were designed in part to remedy the longstanding discrimination between rates charged FX and MTS users, thus satisfying one of the central purposes of this proceeding. As early as the *Second Supplemental Notice* we presented a plan to establish parity between FX and MTS rates. 77 F.C.C.2d 224. The *Access Charge Order* achieved this parity in a way that differed somewhat from the plan described in the *Second Supplemental Notice*. That *Order* required that carrier's carrier charges, including Carrier Common Line charges, be assessed in the foreign exchanges for each minute of use that FX service made of that local network. Petitioners have not demonstrated that FX charges that are lower than OCC charges would be warranted.

Id.

ARINC's argument on appeal is relatively simple. It argues that throughout the FCC's orders there runs the recurring theme that the Commission has been on guard against potentially devastating impacts of the new rate structure upon certain classes of communications consumers. This concern has been embodied in a variety of transitional devices designed to introduce consumers of specified services to the new access charges in stages. "In sharp contrast to its solicitude for the impact of its decision on other entities," ARINC argues, "the agency totally ignored the impact on subscribers of the largest rate increase it prescribed . . .", namely, FX users. Brief for ARINC at 32. "[T]he Commission failed to take into

account the manifest threat to the viability of an industry already under severe financial strain—the airlines," continued ARINC. *Id.* at 33. It concluded:

> The Commission's complete indifference to the plight of FX users facing massive rate increases, in contrast to its oft-repeated solicitude for all other entities facing even a fraction of such an impact, flies in the face of its obligation to deal evenhandedly with different parties who are similarly situated.

Id. at 35. ARINC refers the court to a well-known series of cases which undoubtedly do establish the proposition that an agency must "take pains to reconcile an apparent difference in the treatment accorded litigants circumstanced alike." *Garrett v. FCC*, 513 F.2d 1056, 1060 (D.C.Cir. 1975). *See also Melody Music, Inc. v. FCC*, 345 F.2d 730, 732-33 (D.C.Cir. 1965)

The FCC's response to ARINC's objections is twofold. First, the agency repeats what it has earlier stated in its orders: it must treat FX users as it does the users of MTS/WATS or similar OCC-provided services in order to avoid violating its statutory command of non-discrimination. Second, the Commission points to various aspects of its plan which do take into account concerns for the position of FX subscribers:

> In fact, the Commission did consider the transitional impact on FX customers in designing its access plan. First, FX customers pay only non-premium access rates, even though it costs virtually the same to provide the FX line-side connections as it costs to provide the premium trunk-side connections. . . . Second, the FCC decided to assess the FX non-premium charge on a per minute rather than on a per line basis in order to protect those FX customers with relatively low usage. . . . Third, the Commission has recognized the "substantial hardship" that low-volume FX customers might suffer in areas in which no FX usage measurement capability now exists. . . . The FCC refused to allow carriers in such areas to charge a flat FX rate based on a monthly minute

> count of 4,076, which the FCC viewed as too high. Instead, the Commission permitted carriers to charge the equivalent of the local business rate, or to develop some other reasonable surrogate charge. . . These measures show that while the FCC may not have gone as far as ARINC might have liked, ARINC is certainly wrong to assert that the Commission entirely ignored the impact on FX customers of the new access rates.

Brief for the FCC at 106-108.

We begin by noting that the FCC's first order in this matter appeared on March 11, 1983. The new plan will take effect, at the earliest, in June of 1984. Thus *every* subscriber to *any* service which will be assessed an increase in cost due to access charges will have in effect enjoyed a minimum period of transition of more than a year. This does not even include the far longer period of time beginning with the *Second Supplemental Notice* in April of 1980 when notice was first given that the FCC intended to remedy the discrimination in rates between MTS, OCC and FX users. *Second Supplemental Notices,* 77 F.C.C.2d 224 (1980). Charges that the FCC has acted precipitously with regard to any class of user simply do not wash. Exclamations of "rate shock" are similarly undermined when the period since first notice has itself become a protracted delay.

Second, the court need not accept AT&T's characterization of FX users as that category of users "who, more than any other class of users, have escaped responsibility for massive interstate use of local facilities," Brief for AT&T at 54, to nevertheless conclude that FX subscribers have been enjoying very advantageous benefits for many years. The size alone of the airlines' FX network is eloquent testimony of advantages enjoyed by FX users over consumers of other means of interstate connection. FX service appears to be the functional equivalent of standard long-distance and like services. Nothing in the

record indicates that FX customers using FX service deserve any better treatment than customers of those other services who will ultimately be required to bear the cost of the new access chargs. FX customers have in the past enjoyed what amounted to a subsidy paid for by other long distance users.

Third, we are impressed with those features of the FCC's plan that do cushion the blow for FX users. Indeed, we are hard pressed to understand why FX users are not being charged the premium rate for access as MTS customers, unless the FCC in fact gave some consideration to the rate shock which FX users will feel when introduced to the new order.

We must reject ARINC's attempt to reclassify FX as something other than the equivalent of MTS (long distance) service. ARINC shrewdly attempts to obscure obvious differences between FX and other services such as PBX and Centrex-Co and then to argue that it deserves every consideration shown these categories of services. There are substantial differences. Throughout this proceeding the FCC has taken great pains to draw a great number of careful and often subtle distinctions. It has done so here as well. ARINC urges the court to redraw the lines and shuffle the categories—a chore for which we are manifestly not suited. While the court is most certainly "not a hostile stranger to the office of first instance",[43] neither is it the draftsman of intricate new plans.

We must also point out that it is possible both to accept the accuracy of ARINC's portrayals of the cost impact about to hit the airlines and to dismiss that consideration as irrelevant. Woven into ARINC's brief is the theme that, somehow, the airlines are different. But, so far as this appeal is concerned, they are not. ARINC could not seriously argue that the impact upon a single industry of the FCC's vast and ambitious reworking of the com-

[43] Greater Boston Television Corporation v. FCC, 444 F.2d 841, 852 (D.C. Cir. 1970), *cert. denied,* 403 U.S. 923 (1971).

munications industry's rate structure could in any way affect the outcome of our review. There are winners and losers galore as a result of the FCC's plan which will eventually place the cost of services provided upon those who use the facilities. It is certainly not within the scope of this court's review to seize upon the impact on a single industry as a reason for returning the FCC to its drawing board. Consideration of the FX-connected question places us in the center of the FCC's ambit of discretionary authority. Accordingly, we affirm this segment of its plan.

III. CONCLUSION

Over five years' study of complex and far-ranging issues set the foundation for the FCC's orders in this case. The Commission predicted industry trends and the impact of rate changes, reconciled widely diverse policy goals and numerous competing interests, and devised solutions to novel and difficult problems. Confronting rapid and fundamental changes in the telephone industry as a result of competition and fast-moving technology, the FCC acted for the most part with flexibility and care. The Commission's work fell short of the ideal at several turns, but our review does not and cannot require perfection. *See MCI Telecommunications Corp. v. FCC*, 627 F.2d 322 (D.C. Cir. 1980); VOLTAIRE, DICTIONNAIRE PHILOSOPHIQUE (Dramatic Art) (1794) ("Le mieux est l'ennemi du bien"—the best is the enemy of the good).

We do not find unreasoned the Commission's determination that, to the extent practical, telephone prices should be "based upon the true cost characteristics of telephone company plant." *Access Order* ¶ 28, 93 F.C.C.2d at 251. Nor, with limited exceptions, can we quarrel with the FCC's exercise of judgment in deriving workable formulas, estimating numbers that cannot be mathematically proved, and making equitable assessments of the speed with which changes should be introduced.

Further refinements to the FCC's plan could be debated endlessly. However, the Commission has reached a point in its deliberations where "a month of experience will be worth a year of hearings." *American Airlines, Inc. v. CAB*, 359 F.2d 624, 633 (D.C. Cir.), *cert. denied*, 385 U.S. 843 (1966). The FCC has not achieved a plan of pristine quality. But "[i]n the words of Voltaire: Perfection is attained by slow degrees; it requires the hand of time." *Access Order*, 93 F.C.C.2d at 364 (statement of Commissioner Quello).

For the reasons stated, we affirm the Commission's orders in principal part, and remand for further consideration consistent with this opinion the segments on party line service and small telephone companies' election of "average schedule company" status.

It is so ordered.

APPENDIX B

STATUTES & REGULATIONS

47 U.S.C. sec. 152(b)

(b) Except as provided in section 224 of this title and subject to the provisions of section 301 of this title, nothing in this chapter shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier, or (2) any carrier engaged in interstate or foreign communication solely through physical connection with the facilities of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier, or (3) any carrier engaged in interstate or foreign communication solely through connection by radio, or by wire and radio, with facilities, located in an adjoining State or in Canada or Mexico (where they adjoin the State in which the carrier is doing business), of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier, or (4) any carrier to which clause (2) or clause (3) of this subsection would be applicable except for furnishing interstate mobile radio communication service or radio communication service to mobile stations on land vehicles in Canada or Mexico; except that sections 201 to 205 of this title shall, except as otherwise provided therein, apply to carriers described in clauses (2), (3), and (4) of this subsection.

(As amended Feb. 21, 1978, Pub.L. 95-234, § 5, 92 Stat. 35.)

47 U.S.C. sec. 221(b)

(b) Subject to the provisions of section 301 of this title, nothing in this chapter shall be construed to apply, or to give the Commission jurisdiction, with respect to charges, classifications, practices, services, facilities, or regulations for or in connection with wire, mobile, or point-to-point radio telephone exchange service, or any combination thereof, even though a portion of such exchange service constitutes interstate or foreign communication, in any case where such matters are subject to regulation by a State commission or by local governmental authority.

47 U.S.C sec. 410(c)

(c) Federal-State Joint Board; reference of proceedings regarding jurisdictional separation of common carrier property and expenses between interstate and intrastate operations and other matters relating to common carrier communications of joint concern; jurisdiction, powers, duties, and obligations; recommendation of decisions; State members; presence at oral arguments and nonvoting participation in deliberations; composition; Chairman

The Commission shall refer any proceeding regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations, which it institutes pursuant to a notice of proposed rulemaking and, except as provided in section 409 of this title, may refer another matter, relating to common carrier communications of joint Federal-State concern, to a Federal-State Joint Board. The Joint Board shall possess the same jurisdiction, powers, duties, and obligations as a joint board established under subsection (a) of this section, and shall prepare a recommended decision for prompt review and action by the Commission. In addition, the State members of the Joint Board shall sit with

the Commission en banc at any oral argument that may be scheduled in the proceeding. The Commission shall also afford the State members of the Joint Board an opportunity to participate in its deliberations, but not vote, when it has under consideration the recommended decision of the Joint Board or any further decisional action that may be required in the proceeding. The Joint Board shall be composed of three Commissioners of the Commission and of four State commissioners nominated by the national organization of the State commissions as referred to in sections 302(b) and 305(f) of Title 49, and approved by the Commission. The Chairman of the Commission, or another Commissioner designated by the Commission, shall serve as Chairman of the Joint Board.

(As amended Sept. 30, 1971, Pub.L. 92-131, § 2, 85 Stat. 363.)

(8)

NO. 84-95

In the Supreme Court of the United States

OCTOBER TERM, 1983

NATIONAL ASSOCIATION OF
REGULATORY UTILITY COMMISSIONERS,

Petitioner

v.

FEDERAL COMMUNICATIONS COMMISSION AND
UNITED STATES OF AMERICA

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF OF RESPONDENT DEPARTMENT OF PUBLIC UTILITY CONTROL OF THE STATE OF CONNECTICUT IN SUPPORT OF THE PETITION

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August 9, 1984

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QUESTIONS PRESENTED FOR REVIEW

Congress provided, in the express language of the Communications Act of 1934, that jurisdiction over telecommunications be divided between the Federal Government and the States. The Federal Communications Commission was granted authority over interstate and international communications, 47 U.S.C. §151, while authority over the intrastate sphere was reserved to the States. 47 U.S.C. §§152(b), 221(b). Against this background, the questions presented by the National Association of Regulatory Utility Commissioners are as follows:

1. Whether the decision of the District of Columbia Circuit affirming the FCC's end user access charge plan is consistent with this Court's decision in *Smith v. Illinois Bell* governing the regulatory treatment of local telephone company-owned facilities used for both interstate and intrastate communications?

2. Whether the Court of Appeals for the District of Columbia Circuit erred in concluding that the Federal Communications Commission acted within its statutory authority under the Communications Act of 1934 in promulgating its end user access charge plan?

PARTIES

The parties to the proceeding before the United States Court of Appeals for the District of Columbia Circuit are listed in the Petition for a Writ Certiorari filed by the National Association of Regulatory Utility Commissioners.

The Department of Public Utility Control of the State of Connecticut is the state regulatory agency responsible for ensuring the establishment and operation of such communications services and facilities as may be in the interest of the residents of the State of Connecticut and the furnishing of such service at rates that are just and reasonable.

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In the Supreme Court of the United States

OCTOBER TERM, 1983

NO. 84-95

NATIONAL ASSOCIATION OF
REGULATORY UTILITY COMMISSIONERS,

Petitioner

v.

FEDERAL COMMUNICATIONS COMMISSION AND
UNITED STATES OF AMERICA

Respondents.

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*ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT*

BRIEF OF RESPONDENT DEPARTMENT OF PUBLIC UTILITY CONTROL OF THE STATE OF CONNECTICUT IN SUPPORT OF THE PETITION

The Department of Public Utility Control of the State of Connecticut submits this brief in support of the petition for a writ of certiorari filed by the National Association of Regulatory Utility Commissioners (NARUC).

OPINIONS BELOW

The opinion of the United States Court of Appeals for the District of Columbia Circuit is set forth in NARUC Appendix A.

The Federal Communications Commission's access charge order is reported at 93 FCC2d 241 (1983). Its order on initial reconsideration is reported at 48 Fed. Reg. 42, 984 (1983). Its order on further reconsideration is reported at 49 Fed. Reg. 7, 810 (1984).

JURISDICTION

The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1). The decision of the Court of Appeals for the District of Columbia Circuit was entered on June 12, 1984. The petition for a writ of certiorari was filed by NARUC on July 18, 1984, within 90 days of the decision of the Court of Appeals. NARUC's petition was received by the Department of Public Utility Control of the State of Connecticut on July 23, 1984. This brief is filed within 20 days of that date.

STATUTES AND REGULATIONS

47 U.S.C. §151 is set forth in Appendix A. 47 U.S.C. §152(b) is set forth in NARUC Appendix B.

STATEMENT OF THE CASE

The Department of Public Utility Control adopts the statement of the case set forth in NARUC's petition.

SUMMARY OF THE ARGUMENT

The Federal Communications Commission, by its Access Charge Order, imposed a flat rate charge on telephone end users to recover the interstate portion of the costs associated with the local telephone loop. That charge is imposed on telephone subscribers regardless of whether any use is made of the interstate network and is a condition precedent to the receipt of basic, intrastate service. The access charge order violates the provisions of the Communications Act of 1934, §§47 U.S.C. 151 and 152(b).

1. The direct result of the access charge is to decrease the affordability of basic, intrastate telephone service to the vast majority of telephone customers. This result violates the FCC's primary mission under the Communications Act of 1934 to make basic telephone service available, "as far as possible, to all the people of the United States." 47 U.S.C. 151. The Court of Appeal's failure to review the FCC's administrative action in light of the agency's fundamental statutory directive constitutes serious error.

2. The access charge, imposed as a precondition to the receipt of basic, intrastate telephone service, violates the Congressional division of jurisdiction over the national communications network between the FCC and the States set forth in 47 U.S.C. 152(b). The Court's failure to properly assess Congress's reservation of authority over intrastate service to the States and the FCC's violation of that authority is contrary to the decisions of this Court.

REASONS FOR GRANTING THE WRIT

In recent years, the Federal Communications Commission (FCC) has been changing the way America makes and pays for its telephone service.[1] This process, joined with the breakup of AT&T,[2]

[1]The FCC opened interstate telephone service to competition between AT&T and other common carriers (OCC's) *MTS & WATS Market Structure: Report & Third Supplemental Notice of Inquiry*, 81 FCC 2d 177, 183 (1980) (*Third Supplemental Notice*); detariffed customer premises equipment (CPE) preempting all state rate regulatory authority *In re Amendment of §64.702 of the Commission's Rules and Regulations (Second Computer Inquiry)* 77 FCC 2d 384 (1980) and removed the provision of enhanced telephone services from state supervision. *Memorandum Opinion and Order, In re Amendment of §64.702 (Second Computer Inquiry)* 84 FCC 2d 50 (1980).

[2]*United States v. American Telephone and Telegraph Co.*, 552 F.Supp. 131 (D.D.C. 1982).

peaked with the FCC's decision to impose a flat-rate charge on all local telephone subscribers—the access charge—for their enjoyment of the opportunity to use the interstate telephone network. *MTS & WATS Market Structure: Third Report & Order,* 93 FCC 2d 241 (1983) (*Access Charge Order*).

While framed in terms of economic theory, cost causation and revenue collection, the access charge decision represents more than a mere restructuring of telephone rates and telephone service expense allocation. The charge represents a serious departure from the FCC's primary statutory mission under the Communications Act of 1934 "to make available, so far as possible, *to all the people of the United States,* a rapid, efficient, Nationwide . . . wire and radio communication service . . .". 47 U.S.C. 151 (emphasis supplied). With its access charge order—the culmination of a series of detariffing, deregulation and preemption decisions—the FCC has struck at the heart of the Communications Act.

A. *The Access Charge Order Impairs the Goal of Universal Service Mandated by the Communications Act of 1934.*

The nationwide telephone system—in service, costs and revenues—is divided between the interstate and intrastate jurisdictions. Between the two are the nontraffic sensitive costs (NTS) of the local loop connecting the subscriber to both networks. After *Smith v. Illinois Bell Telephone Company,* 282 U.S. 133 (1930) the interstate portion of the local NTS costs were apportioned to, and collected from, telephone customers on a per call basis as use was made of the interstate system. That arrangement looked to the totality of the local NTS plant in its cost and in its revenue recovery, recognizing the value to long distance service of an extensive local network as an outlet for interstate traffic. As customer contributions to the local system's interstate costs were on a usage basis, basic intrastate telephone service was made affordable and, thus, available, "so far as possible, to all the people of the United States . . ." 47 U.S.C. 151. The Court of Appeals recognized, albeit in a different

context, that cost recovery on a usage basis was a "neutral, reasonable principle" (*NARUC v. FCC*, No. 83-1225, slip op. at 80, NARUC Appendix at 80a) in the collection of NTS costs:[3]

> "(W)hen charges are grounded in relative use, a single rate can produce a wide variety of charges for a single service, depending on the amount of service used. Yet there is no discrimination among customers, since each pays equally according to the volume of service used.... Although OCC's will pay many more dollars per line for access charges, they require and use a correspondingly higher volume of exchange access on each line."

NARUC v. FCC, supra, slip op. at 80, NARUC Appendix A at 80a.

With its access charge order, however, the FCC moved away from its responsibility to increase the availability of basic telephone service to *all* the people of the United States. The access charge is to be imposed as a precondition to receipt of basic local service without regard to whether any use is made of the interstate network. As such, it will raise an entry barrier to the receipt of *any* telephone service. As the charge was designed, very specifically, to benefit only high-use interstate telephone customers, to the vast majority of present and would-be telephone users, the affordability of any telephone service is decreased. Lower per-minute interstate rates are not in the public interest when the cost of basic telephone service is prohibitive.

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[3]The Court of Appeals found that the "temporary" recovery of a portion of the local loop NTS costs from common carriers on a usage basis was proper because it promotes "economic efficiency". *NARUC v. FCC*, No. 83-1225, slip op. at 83 (D.C. Cir. June 12, 1984); NARUC Appendix A at 83a. The Court's sustaining the FCC's opposite conclusion in terms of end users stands the Communications Act on its head. The Act was adopted to make telephone service *available*, "as far as possible", to *all* people—not to make it as "economically efficient," as far as possible, and available only to some.

Generally speaking, the FCC has broad discretion to determine where the public interest lies. *FCC v. WNCN Listeners Guild*, 450 U.S. 582 (1981). The agency's assessment of the public interest, however, must at least be founded upon the appropriate statutory standards.[4] *FCC v. Midwest Video*, 440 U.S. 689, 706-708 (1979). Although *Smith v. Illinois Bell, supra*, does not dictate the exact retention of the historical system of interstate cost collection, the Communications Act does require that any new approach promote, rather than impair, universal service. Even if a new direction can be achieved only by balancing competing considerations, the FCC's primary responsibility rests with increased basic service availability.[5] Cf. *Motor Vehicle Manufacturers Ass'n v. State Farm Mutual*, 103 S.Ct. 2856, 2873 (1983) In this case, however, the FCC did not act to increase the availability of basic telephone service, the FCC sacrificed it to "economic efficiency".[6]

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[4]In its *Memorandum Opinion and Order, MTS AND WATS Market Structure*, 48 Fed. Reg. 42, 984 (1983) (*Reconsideration Order*), the FCC explains the "driving force" behind its access charge decision.¶¶ 7, 48 Fed. Reg. 42, 986. It is noteworthy that the FCC's statutory mandate to increase the affordability and availability of telephone service "to all the people of the United States" is not mentioned.

[5]The threat of uneconomic bypass was raised by the FCC and the Court of Appeals as a consideration virtually dictating the imposition of the end user access charge. That conclusion is erroneous. Residential customers do not have to pay an access charge to avoid the effects of uneconomic bypass. Other methods of effectively dealing with uneconomic bypass which would not impair the availability of basic telephone service were presented to the Commission. These, however, were rejected because they were not as "economically efficient" as the end user charge.

[6]Interestingly enough, the level of interstate costs on which the access charge is to be determined is not set on a nontraffic sensitive basis. Under the FCC's most recent NTS allocation decision 75% of the local NTS costs are assigned to the intrastate network and only 25% to the interstate—an approximation of the relative use between the two jurisdictions. *Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, 49 Fed. Reg. 7934 (1984). Under the end user access charge rationale—that cost causation does not depend on the number of calls

The FCC's only response to its primary statutory purpose was a belated attempt to mitigate the damage which the access charge will have on universal service. Instead of adopting a policy which would benefit basic telephone service, the FCC tacked onto its access charge a Universal Service Fund,[7] a transition plan to periodically raise the charge until it reaches full NTS cost recovery, a study and the possibility of life line waivers. *Memorandum Opinion and Order, MTS and WATS Market Structure ¶¶5, 11-14, 48 Fed. Reg. 42, 984, 42, 986-987 (1984) (Reconsideration Order).* The FCC's attempts to mitigate the damage occasioned by its access charge simply do not qualify as affirmative attempts to increase telephone availability as required by the Communications Act. If anything, such steps demonstrate that, in what the FCC has described as perhaps its "most important" decision concerning the future of the nation's telephone system[8], the agency has abandoned its primary statutory directive.

In this regard, the Court of Appeals review of the FCC action was wholly inadequate. The Court turned a blind eye to the deleterious impact of the access charge on the availability of basic telephone service. The Court reasoned that as the transitional plan to full cost recovery requires that only "some" of the NTS costs are to be recovered now, the FCC charge is valid because it will not immediately have a "substantial negative effect" on universal service.

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made—the NTS costs should be divided on a 50-50 basis. It would appear that with its transitional implementation plan and its current allocation scheme the FCC, at this point, is content to hide the full effect of "economic efficiency" from the public.

[7]Despite its name, the Universal Service Fund is not designed to promote universal service. It does nothing to reduce the deleterious impact of the access charge's recovery of all interstate NTS costs except where the end user charges in high cost areas *exceed, by several times,* the nationwide average charges. *Reconsideration Order, supra,* ¶¶11, 48 Fed. Reg. at 42, 987.

[8]*MTS & WATS Market Structure: Third Report and Order,* 93 F.C.C. 2d 241, 340-341 (1983).

NARUC v. FCC, supra, slip op. at 52, NARUC Appendix at 52a. The Court's rationale is erroneous for several reasons.

First, the Court in a different part of its decision admitted that the end user access charge is designed to eventually reach complete NTS cost recovery.[9] The fact that the access charge damage to universal service is designed to increase in intensity over time does not mean that the charge, in its initial stages, is consistent with the goals of the Communications Act. The Court's present failure to address the conflict between the access charge and universal service makes any future increase in that charge essentially unreviewable.

Second, the universal service provision of the Communications Act is not drafted in the negative. The FCC was created with the *affirmative* duty of increasing the availability of telephone service and the FCC's action should have been measured against that requirement. Cf. *American Textile Manufacturers Institute v. Donovan,* 452 U.S. 490, 508-514, 540-541 (1981). The Court's employment of a "no substantial negative effect" standard to review the FCC decision in this case contradicts the plain wording of 47 U.S.C. 151. The Court's failure to properly consider the basic purpose of the Communications Act as a directive for FCC administrative action constitutes serious error.

B. *The Access Charge Order Impermissibly Impairs Intrastate Telephone Service.*

Section 2(b) of the Communications Act of 1934 explicitly states that the Commission shall not have jurisdiction with respect to

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[9]In discussing the transitional nature of the collection of interstate NTS costs under the common carrier charge the Court noted:

> "The inside wiring and customer premises equipment costs will be gradually removed from the rate base, and the balance of NTS exchange costs not recovered from end users or through the Universal Service Fund will probably drop to zero." *NARUC v. FCC, supra,* slip op. at 73, NARUC Appendix at 73a.

"charges, classifications, practices, services, facilities or regulations for or in connection with intrastate communication service by wire or radio of any carrier." Under the access charge, however, receipt of basic, intrastate service is conditioned upon payment of interstate costs regardless of use of the interstate network. As the FCC has conditioned receipt of intrastate service on its access charge, it has seized jurisdiction over the provision of intrastate service, in violation of 47 U.S.C. 152(b).

The Court of Appeals in reviewing the impact of the access charge on intrastate service held that the FCC had jurisdiction to collect interstate charges in any manner that it chose. The Court relied upon its decision in *Computer and Communications Industry Association v. FCC,* 693 F2d 198 (D.C. Cir. 1982), *cert. denied,* 103 S.Ct. 2109 (1983) (*Computer II*), for the proposition that, under general preemption principles, the FCC has plenary authority over any aspect of the communications network which involves both interstate and intrastate service.

Such general principles, however, completely write §2(b) out of the Communications Act. The statutory limitation on FCC jurisdiction must have some meaning. Yet it has none if receipt of basic, intrastate service depends upon the fulfillment of FCC conditions precedent.

The Court of Appeals decision violates the principles set forth in this Court's decision in *Pacific Gas & Electric Company v. State Energy Resources Conservation and Development Commission,* 103 S.Ct. 1713 (1983). In that case this Court noted that the Atomic Energy Act of 1954 contained an express reservation of authority to the States to regulate the nuclear power industry "for purposes other than protection against radiation hazards." 42 U.S.C. §2021(k). Because of that reservation this Court held that a California statute conditioning certification of nuclear plants on the development of a demonstrated technology for the disposal for nuclear waste was not preempted by the authority of the Nuclear Regula-

tory Commission. The statutory reservation of authority to the States in 42 U.S.C. §2021(k) established a boundary line for judging a state's interference with the accomplishment and execution of the full purposes and objectives of Congress.

Similarly, a statutory reservation of authority to the States establishes a boundary line beyond which a federal regulatory agency cannot pass to accomplish the full purposes and objectives of Congress. This is so because a reservation of authority to the States establishes one of Congress's objectives.

In this case a reservation of State authority over intrastate telephone service is contained in §47 U.S.C. 152(b). Although collection of the interstate costs of the local loop may fall within the jurisdiction of the FCC, §47 U.S.C. 152(b) prohibits the FCC from conditioning the receipt of basic, intrastate service on such charges. The FCC's access charge decision plainly violates the division of regulatory authority between the Commission and the States set forth in the Communications Act of 1934.

> "The Court of Appeals is right, however, that the promotion of nuclear power is not to be accomplished 'at all costs.' The elaborate licensing and safety provisions and the continued preservation of state regulation in traditional areas belie that . . . . the legal reality remains that Congress has left sufficient authority in the states to allow the development of nuclear power to be slowed or even stopped for economic reasons. Given this statutory scheme, it is for Congress to rethink the division of regulatory authority in light of its possible exercise by the states to undercut a federal objective. The courts should not assume the role which our system assigns to Congress."

Pacific Gas & Electric Co. v. State Energy Resources Conservation and Development Commission, supra, 103 S.Ct. 1713 at 1731-32.

CONCLUSION

For the reasons set forth herein, the Department of Public Utility Control of the State of Connecticut prays that a writ of certiorari be issued to the United States Court of Appeals for the District of Columbia Circuit.

Respectfully submitted,

The Department of
Public Utility Control
of the State of Connecticut

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August 9, 1984

In the Supreme Court of the United States

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NO. 84-95

NATIONAL ASSOCIATION OF
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*ON PETITION FOR A WRIT OF CERTIORARI
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APPENDIX TO THE BRIEF OF RESPONDENT DEPARTMENT OF PUBLIC UTILITY CONTROL OF THE STATE OF CONNECTICUT IN SUPPORT OF THE PETITION

APPENDIX A

47 U.S.C. §151. Purposes of chapter; Federal Communications Commission created.

For the purpose of regulating interstate and foreign commerce in communication by wire and radio so as to make available, so far as possible, to all the people of the United States a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges, for the purpose of the national defense, for the purpose of promoting safety of life and property through the use of wire and radio communication, and for the purpose of securing a more effective execution of this policy by centralizing authority heretofore granted by law to several agencies and by granting additional authority with respect to interstate and foreign commerce in wire and radio communication, there is created a commission to be known as the "Federal Communications Commission", which shall be constituted as hereinafter provided, and which shall execute and enforce the provisions of this chapter.

No. 84-95

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS,
Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION and UNITED STATES OF AMERICA, *et. al.,*
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF IN OPPOSITION FOR MCI TELECOMMUNICATIONS CORPORATION

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TABLE OF AUTHORITIES

LIST REQUIRED BY RULE 28.1

Respondent MCI Telecommunications Corporation is wholly owned by MCI Communications Corporation. Other companies owned by MCI Communications Corporation are: American Television Relay, Inc.; British Western Union, Ltd.; Consolidated Communications Supply Company, Inc; MCI Airsignal, Inc.; MCI Airsignal Leasing, Inc.; MCI Airsignal of California, Inc.; MCI Airsignal of Colorado, Inc.; MCI Airsignal of Indiana, Inc.; MCI Airsignal of Nevada, Inc.; MCI Airsignal of Philadelphia, Pennsylvania, Inc.; MCI Airsignal of Pittsburgh, Pennsylvania, Inc.; MCI Airsignal of Virginia, Inc.; MCI Akron Cellular, Inc.; MCI Carolina Cellular, Inc.; MCI Cellular Systems, Inc.; MCI Cellular Telephone Company; MCI Charlotte Cellular, Inc.; MCI Cleveland Cellular, Inc; MCI Data Processing, Inc.; MCI Data Transfer Corporation; MCI Denver Cellular, Inc.; MCI Digital Information Services Corporation; MCI Equipment Corporation; MCI Galaxy III Transponder Leasing, Inc.; MCI International Telecommunications Corporation; MCI International, Inc.; MCI Kansas City Cellular, Inc.; MCI LA Cellular, Inc.; MCI LAX Corporation; MCI Leasing, Inc.; MCI Memphis Cellular, Inc.; MCI Message Network, Inc.; MCI Minnesota Cellular, Inc.; MCI Norfolk Cellular, Inc.; MCI Oklahoma Cellular, Inc.; MCI Philadelphia Cellular, Inc.; MCI Raleigh Cellular, Inc.; MCI Realty Corporation; MCI Services Corporation; MCI Sharing Services, Inc.; MCI Telecommunications Corporation; MCI Telecommunications Corporation of Virginia; MCI Transponder Leasing, Inc.; MCI Virginia Cellular, Inc.; MCI/TAS Corporation; N-Triple-C Inc.; Transatlantic Cable, Ltd.; WUI Dataprocessing Corporation; WUI Sales Corporation; WUI Service Corporation; WUI Specialized Communications, Inc.; Western Union International Caribbean, Inc.; Western Union International, G.M.B.H.; Western Union International, Inc.; Western Union International, S.A.; Western Union International, S.r.l.

STATEMENT OF THE CASE

The Federal Communications Commission ("FCC") decided how interstate telephone rates should be structured in order to recover costs which are subject to its jurisdiction. Its decision was affirmed by the D.C. Circuit. Neither the amount of these costs nor the FCC's jurisdiction over these costs is contested by the Petitioner, National Association of Regulatory Commissioners ("NARUC"). The subject of its petition is the interstate rate designed to recover the interstate costs of the local telephone company line which connects a residence or business to the local telephone company switch.[1] Such lines are used for both local exchange and intrastate long distance, and interstate long distance calling. Under a formula agreed to by a Joint Board of state PUC and FCC commissioners—a formula which is not at issue in this case—approximately one quarter (1/4) of the costs of such local lines have been allocated to the interstate jurisdiction for recovery through interstate rates.[2] The costs of these lines are non-traffic sensitive so that they remain exactly the same whether the telephone subscriber makes 1000 interstate and local calls a month or makes no calls whatsoever.[3] The Commission found that in order to be cost-based, the interstate rate for these lines, like their costs, should not vary with usage.[4] It found that the rate should be the responsibility of each subscriber because he has imposed the costs upon the network by ordering a line connecting his premises to the local telephone company switch.[5] Therefore, the Commis-

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[1]These costs include the costs of the line itself, as well as the costs of terminals and other customer premises equipment, the protection block and drop wire. *MTS and WATS Structure: Third Report and Order*, 93 FCC 2d 241, 269 (1983) *(Access Order)*.

[2]*NARUC v. FCC*, No. 83-1225, slip op. at 22 (D.C. Cir. June 12, 1984).

[3]*Id.*, slip op. at 19-20.

[4]*Id.*, slip op. at 29-30.

[5]*Id.*, slip op. at 29.

sion ordered that these non-traffic sensitive costs be recovered from the subscriber through flat rates,[6] rather than by usage-sensitive toll rates.[7]

The Commission's cost-based rate structure has the potential to liberate the nation's communications system from the previous exclusive reliance on artificially high usage-sensitive rates.[8] As non-traffic sensitive costs are recovered through flat rates, per minute rates for individual calls will decrease and usage of the nation's phone system will no longer be artificially repressed. Continued long-run reliance upon usage-based prices for the recovery of all non-traffic sensitive costs would artificially restrict calling patterns, distort economy-wide investment decisions, and even jeopardize the competitive position the U.S. now holds in the world marketplace.[9] The development of computer and related technologies could be inhibited.[10] The Commission's cost-

[6]A flat fee for multi-line business customers is currently in effect at a rate of approximately $6/line. Residential and single-line business customers are expected to be assessed a flat rate starting in mid-1985. The initial amount of the rate has not been set although the Commission has determined that it should not exceed $4/line through 1990. *NARUC v. FCC*, slip op. at 31-32.

[7]*Id.*, slip op. at 29-30. Other interstate costs would be recovered from subscribers through per minute rates. The per minute interstate rates are not the subject of the petition for certiorari. Under the FCC's plan, per minute rates would be assessed against telephone users in much the way they are now, so that rates for individual calls would be based on the duration of the call and the distance over which the call is transmitted. While all telephone subscribers will pay the flat interstate rate, some large volume subscribers and subscribers to interstate private lines will not pay a strict per minute rate but instead will be subject to specialized rate structures.

[8]*NARUC v. FCC*, slip op. at 29-30.

[9]*Access Order*, 93 FCC 2d at 275 (1983).

[10]*Id.* at 274, n.37.

based rate structure also has the potential to preserve the affordability of basic telephone service over the long term by preventing the defection of large telecommunications users from the local telephone network.[11] Without cost-based pricing, those large users have a strong economic incentive to "by-pass" the local telephone companies with facilities of their own. The remaining subscribers would then have to pay higher rates to replace the lost revenues previously provided by the large users.[12]

The Commission took a number of steps to ensure that its new combination of flat and usage-sensitive rates would not adversely affect the opportunity for universal telephone service in the short term. The Commission set up a universal service fund whereby interstate carriers would be obligated to bear a portion of the NTS costs so that the flat charge against the telephone user could be reduced in certain high cost areas.[13] The flat charge to the subscriber is to be phased in over time with a maximum "cap" of $4 for residential and single line customers until at least 1990.[14] The Commission staff was instructed to develop a monitoring program to detect any unanticipated effects of access charges upon subscriptions to telephone service, and the Commission promised to conduct a further proceeding before permitting residential rates in excess of $4 per month.[15] The Commission is conducting proceedings to devise a rule that would provide an exemption from the interstate flat charge for those

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[11]*NARUC v. FCC*, slip op. at 29.

[12]*Id.* at 22 and 29.

[13]*Further Reconsideration Order* at para. 8, 55 RR 2d (P&F) 785, 789, 49 Fed. Reg. 7810, 7811 (1984).

[14]*Id.* at para. 20, 55 RR 2d at 791, 49 Fed. Reg. at 7812. *See also NARUC v. FCC*, slip op. at 32.

[15]*Further Reconsideration Order* at para. 9, 55 RR 2d (P&F) at 789, 49 Fed. Reg. at 7811.

persons (if any) who might have to disconnect if required to pay the flat charge.[16] The Commission is also examining waiver procedures for small telephone companies so that they could be exempt from the requirement of imposing full flat charges.[17]

SUMMARY OF ARGUMENT

NARUC seeks to turn a question of rate structure policy into a legal issue by asserting that the FCC and the court below have violated *Smith v. Illinois Bell,* 282 U.S. 133 (1930). But *Smith* dealt only with the issue of how costs should be separated between the jurisdictions. It did not address the issue of how the rates should be structured once that separation has taken place. Because NARUC here accepts the separations process and challenges only the Commission's rate structure, *Smith* is irrelevant to NARUC's concerns. The allegedly violated "mandate" of *Smith* with respect to intrajurisdictional rate structure simply does not exist. NARUC provides no reference to the place in *Smith* where such a "mandate" is articulated, and claims only that the "mandate" exists by virtue of Smith's "nature." It describes the so-called mandate in terms not used by the *Smith* Court and tries to base it upon fundamental misstatements of fact and economic theory.

Neither is there substance to NARUC's claim of an unlawful prescription by the FCC of an intrastate rate. The

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[16] *Id.* at para. 18, 55 RR 2d (P&F) at 791, 49 Fed. Reg. at 7812.

[17] *Id.* at para. 24, 55 RR 2d (P&F) at 792, 49 Fed. Reg. at 7813. It is questionable whether all of these safeguards are necessary or proper. Nevertheless, it is apparent that the FCC has gone to great lenghts to accommodate the concerns about universal service voiced by parties such as NARUC.

rates prescribed by the FCC were interstate and were designed to recover interstate costs. They are charged to persons that have been provided interstate facilities. Moreover, a consistent line of cases, from which this Court has refused to grant *certiorari*, has held that the FCC has authority over facilities which are used for both intrastate and interstate communications.

ARGUMENT

I. THERE IS NOT EVEN A COLORABLE VIOLATION OF *SMITH v. ILLINOIS BELL*

There is no colorable basis for NARUC's claim of inconsistency between the decision of the D.C. Circuit and the decision of this Court in *Smith v. Illinois Bell.*[18] *Smith* is a jurisdictional separations case and not a rate structure case. *Smith* dealt only with the manner in which the costs of commonly used plant must be separated between the jurisdictions. It did not address how rates should be set to recover those costs once separation has taken place. NARUC does not claim that the costs of commonly used plant have been improperly separated and, indeed, accepts the costs allocated to the interstate jurisdiction as being in conformance with *Smith*. Having accepted those assumptions, NARUC has reached the boundaries of *Smith*. Its claim that

[18]282 U.S. 133 (1930). In *Smith* the Court was faced with a claim that the intrastate telephone rates for coin box service in Chicago set by the state regulatory agency were unreasonably low. Following the *Minnesota Rate Cases, Simpson v. Shepard*, 230 U.S. 352 (1913), the Court found that jointly used telephone property must be separated between the two jurisdictions in order to assess the reasonableness of the state-imposed rates and to maintain the dual jurisdictional scheme established by Congress. There are two basic legal standards which the Court imposed on the separations process. First, the Court held that the separation of jointly used telephone property must be accomplished on a reasonable basis. While the Court recognized the "difficulty in making an exact apportionment," it nevertheless found that "reasonable measures" were "essential." 282 U.S. at 150. Second, the Court found that, in order to

the Commission's rate structure decision violates *Smith* is "exorbitant"[19] simply because it presumes a Supreme Court ruling which was never made on an issue which was never presented.

NARUC claims *Smith* imposes two requirements.[20] The first requirement—that there be an allocation of jointly used property between the jurisdictions—is supported in NARUC's petition with a quotation from *Smith* and an accompanying page citation.[21] NARUC does not claim that this require-

maintain the statutory scheme enacted by Congress, the separations process must not be intended as, nor result in, a subsidy to either of the jurisdictions. The Court emphatically held that the separation of interstate and intrastate property "is essential to the appropriate recognition of the competent government authority in each field of regulation." 282 U.S. at 148. It follows that each jurisdiction must stand independently and may not rely on the ratepayers in the other jurisdiction for support. In applying this principle the Court stated:

> The [Illinois regulatory] commission would have had no authority to impose intrastate rates, if as such they would be confiscatory, on the theory that the interstate revenue of the company was too small and could be increased to make good the loss.

282 U.S. at 148-149. The Court thus declared that the Illinois Commission could not set confiscatorily low intrastate rates on the theory that Illinois Bell could then go to the Federal agency and get higher interstate rates to make up the revenue deficiency. Chief Justice Hughes later characterized his opinion in *Smith v. Illinois Bell*, as being predicated upon the existence of a situation "where the segregation of properties and business was essential in order to confine the exercise of state power to its own proper province." *Lone Star Gas Co. v. Texas*, 304 U.S. 224, 241 (1938). Not addressed by the Court in *Smith v. Illinois Bell* was the question whether jurisdictional separation must also be required to limit the authority of the Federal agency. *See Colorado Interstate Gas Co. v. Federal Power Commission*, 324 U.S. 581, 589 (1945).

[19]Slip op. at 39.

[20]NARUC Petition at 11-12.

[21]*Id.*

ment has been violated. It is the second purported "requirement" of *Smith* on which NARUC's entire certiorari petition is premised. Yet, for this "requirement," NARUC furnishes no quotation from *Smith* and no citation to the page in *Smith* where the requirement is set forth. NARUC merely asserts that this requirement results from *Smith's* "nature":

> Second, *Smith by its nature* requires that the costs of the jointly-used local exchange property allocated to the interstate jurisdiction be recovered from within the interstate sphere, i.e., from interstate end users or interstate carriers.[22]

NARUC attempts to bolster its "nature" assertion with a footnote alleging that *Smith* "made it clear" that there exist two classes of telephone ratepayers and that interstate costs must be recovered from interstate end users instead of local exchange ratepayers.[23] NARUC fails to give any indication where the *Smith* Court "made clear" such a proposition.

The fact is that *Smith* never used the terms "interstate sphere," "interstate end users" or "local exchange ratepayers." This is because *Smith* was concerned only with the jurisdictional separation of costs—not who should pay those costs once divided. Nor does NARUC ever explain what those terms mean. Indeed, rather than being distinct classes, as asserted by NARUC, interstate and local subscribers are identical persons because subscription to telephone service automatically provides access to both local and interstate service.[24] It is not possible to subscribe just to local exchange service or just to interstate service. Nor, after subscription, is it possible to use one's phone exclusively for local use or exclusively for interstate use because the subscriber does not

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[22] *Id.* (emphasis supplied).

[23] *Id.* at n.18.

[24] *NARUC v. FCC*, slip op. at 40.

control the types of calls which he or she receives.[25] Thus, NARUC's assertion that there are two distinct classes of ratepayers is not only a misreading of *Smith*, but is fundamentally incorrect as a matter of fact.

NARUC does not quarrel with the FCC's authority to assess flat interstate charges against those persons who actually make interstate calls, or to assess flat interstate charges against those who actually receive interstate calls. It asserts that *Smith* is violated *only* when a flat interstate charge is assessed against those who neither make nor receive any interstate calls.[26] In such limited circumstances, NARUC claims that the charge is in reality an intrastate charge and violates *Smith's* "mandate" that interstate costs may only be recovered from those who actually use the interstate system.[27]

NARUC has not shown that its hypothetical class of subscribers, who neither make nor receive interstate calls, exists beyond a *de minimis* level or could even be identified. Even if a customer decided to make no interstate calls, even in emergencies, the customer could not prevent receipt of such calls. Nevertheless, assuming that the hypothetical situation on which all of NARUC's arguments are premised could occur, the local exchange user would receive no benefit under NARUC's reasoning. This is because, under NARUC's reasoning, interstate carriers and their customers should not be assessed any portion of the cost of that exclusively intrastate line—since they make, by the terms of the hypotheses, no use of the line whatsoever. With NARUC's reasoning, therefore, the only users who should be assessed

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[25]Even if exclusive local use were possible, in practice it would be prohibitively complex and inefficient to set rates for individual subscribers on such a basis. Slip op. at 43, n.23.

[26]Slip op. at 42, citing Oral Argument Transcript.

[27]Petition for Certiorari at 14.

the cost of those hypothetical access lines used exclusively for intrastate calling would be the intrastate users themselves.[28] And if the exclusive intrastate users of those lines were required to pay a flat intrastate rate to recover the total cost of their lines, they would end up paying an intrastate rate virtually identical to the combined intrastate/interstate rate resulting from the FCC's plan.

NARUC's assertion that actual interstate use must be a precondition to assessment of an interstate rate also ignores fundamental economic fact. The flat charge reflects costs caused not by a subscriber's actually making or receiving local or interstate calls, but by the subscriber's common connection into the interstate and local network.[29] It is the act of subscribing to the network that imposes the line costs, not using the network. Interstate costs of the subscriber's connection which have been allocated to the interstate jurisdiction through the separations process are real and must be recovered regardless of how many or how few interstate calls a subscriber makes. If a person buys an automobile, his purchase price is the same irrespective to how much he happens to use the automobile. Only usage-sensitive costs such as fuel and maintenance are paid on a usage-sensitive basis. NARUC's only response to the court's and the Commission's reliance on this fundamental economic fact is that "NARUC does not agree with the D.C. Circuit's conclusion that a user incurs intrastate [sic] costs merely by being provided with access to the interstate system regardless

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[28] *NARUC v. FCC*, slip op. at 43.

[29] *Id.* at 29.

of whether he *ever* makes use of the system."[30] No citation to the record is provided, and NARUC makes no attempt to explain the factual or economic basis for its disagreement.

Finally, NARUC points to the legislative history of Section 410(c)[31] of the Communications Act as proof that the Commission's flat interstate charge violates the requirements of *Smith*.[32] But there is no indication in the legislative history cited by NARUC that flat interstate charges would violate *Smith*. The language quoted by NARUC states only what *Smith* held—that procedures for separating plant and expenses between the jurisdictions should be fair and equitable and not result in a subsidy to either jurisdiction. NARUC, however, is not contesting the fairness of the separations procedures by which cost were allocated to the interstate jurisdiction. Like *Smith*, Section 410(c) and its legislative history do not deal with the issue of how those costs should be recovered once they are separated fairly. NARUC finds significance in the statement by one legislator that separations should be accomplished "so that no unreasonable burden will be placed on either the interstate or intrastate users of telephone service."[33] Again, however, this language deals only with the separations process, which is not at issue in this case. Moreover, even if that language had relevance to the structure of interstate rates, the Commission's flat

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[30]Petition for Certiorari at 18, n.20 (existing emphasis). NARUC has misstated the court's conclusion. The subscriber does not "incur" costs because of his access to the telephone network. His act of subscription has caused costs and the separations process has allocated part of these costs to the interstate jurisdiction.

[31]Section 410(c) states:

> The Commission shall refer any proceeding regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations. . . to a Federal - State Joint Board.

[32]Petition for Certiorari at 14-16.

[33]*Id.* at 15.

interstate charge imposes no undue burden on "intrastate users." "Intrastate users," if they exist, pay the flat interstate rate simply because they have ordered a facility which can be used for both intrastate and interstate calling, and the costs of that facility have in part been allocated to the interstate jurisdiction. They bear no undue burden by paying the costs of a facility which they have ordered.

II. THE APPLICATION OF ACCEPTED PRECEDENT BY THE D.C. CIRCUIT DOES NOT PRESENT AN IMPORTANT ISSUE OF LAW WHICH NEEDS TO BE SETTLED BY THE SUPREME COURT

Petitioner NARUC seeks to have this Court examine whether the D.C. Circuit properly interpreted Sections 2(b) and 221(b) of the Communications Act.[34] The court's application of precedent to these two sections does not raise an important issue of federal law. To the contrary, the court's ruling is consistent with a line of cases decided by the First, Second, Fourth and the Fifth Circuits, as well as its own prior decisions.[35] This Court has not granted certiorari in any of these cases.

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[34] *Id.* at 17.

[35] *Puerto Rico Tel. Co. v. FCC*, 553 F.2d 694 (1st Cir. 1977); *New York Tel. Co. v. FCC*, 631 F.2d 1059 (2d Cir. 1980); *North Carolina Utilities v. FCC*, 537 F.2d 787 (4th Cir.), *cert. denied*, 429 U.S. 1027 (1976) ("NCUC I"); *North Carolina Utilities Commission v. FCC*, 522 F.2d 1036 (4th Cir.), *cert. denied*, 434 U.S. 874 (1977) ("NCUC II"); *General Telephone Co. of Southwest v. United States*, 449 F.2d 846 (5th Cir. 1971). *General Telephone Co. of Cal. v. FCC*, 413 F.2d 390 (D.C. Cir.), *cert. denied*, 396 U.S. 888 (1969); and *Computer and Communications Industry Association v. FCC*, 693 F.2d 198 (D.C. Cir. 1982), *cert. denied*, 103 S.Ct. 2109 (1983) ("Computer II").

NARUC relies on Sections 2(b)[36] and 221(b).[37] It claims that the interstate flat rate "amounts" to an additional intrastate rate because local service is preconditioned upon payment of the rate.[38] According to NARUC, the charge therefore violates the Communications Act which reserves authority over intrastate rates to the states. The fundamental fallacy to this argument, of course, is that the FCC's flat rate is an interstate rate. It is designed to recover interstate costs, was prescribed as an interstate rate by the agency with interstate jurisdiction, and is charged to persons that have been provided interstate access through facilities whose costs have in part been allocated to the interstate jurisdiction. That the rate must be paid in conjunction with an intrastate rate in order to obtain access to the telephone network merely reflects the technical reality that a telephone subscriber is connected to both the local and interstate networks via the same line.

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[36]Section 2(b) of the Act, 47 U.S.C. Sec. 152(b), states that the Communications Act does not give the FCC jurisdiction over:

> charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier.

[37]Section 221(b) of the Act, 47 U.S.C. Sec. 221(b), provides that:

> [s]ubject to the provisions of section 301 of this title, nothing in this chapter shall be construed to apply, or to give the Commission jurisdiction, with respect to charges, classifications, practices, services, facilities, or regulations for or in connection with . . . exchange service . . . even though a portion of such exchange service constitutes interstate or foreign communication, in any case where such matters are subject to regulation by a State commission or by local governmental authority.

[38]Petition for Certiorari at 14 and 17-18.

Because the Commission's flat charge is an interstate rate, there is no issue concerning the proper interpretation of the Communications Act, let alone an important issue worthy of Supreme Court consideration.[39] Moreover, even if an issue of federal law were present, the decision below showed that a consistent line of cases have ruled that the FCC has authority over facilities which are used for both intrastate and interstate communications.[40] In each of these cases, this Court has denied petitions for certiorari.[41]

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[39]In a brief in support of Petitioner NARUC, Respondent Department of Public Utility Control of the State of Connecticut ("Connecticut") attempts to raise an issue not presented in the Petition for Certiorari. It claims that the court's decision below was erroneous because it did not adequately review the FCC's order against what Connecticut chooses to refer to as the "universal service mandate" of the Communications Act. Conn. Br. at 7-8. In effect, Connecticut seeks to challenge the court's determination that, in general, the universal service question is not ripe for review because the Commission has not determined the size of the flat charge, the shape of transition or the class of persons affected. Slip op. at 52. As the court stated, when those determinations are made by the agency, interested parties below can seek review of the precise plans of the Commission. *Id.* Such a ripeness decision by the court is not an important issue of federal law that requires this Court's attention.

[40]Slip op. at 40-41.

[41]These cases have also uniformly narrowed the scope of Section 221(b) of the Communications Act to situations not presented by petitioner here. Petitioner's reliance on Section 221(b), without discussion of precedent which is directly adverse to its position, is remarkable. As stated by the court below:

> Section 221(b) is irrelevant to the problem before us; its limitation on Commission regulation of telephone exchange service "was merely intended to preserve state regulation of local exchanges that happen to overlap state lines." *Computer and Communications Indus. Ass'n v. FCC*, 693 F.2d 198, 216 (D.C. Cir. 1982), *cert. denied*, 103 S.Ct. 2109 (1983).

Slip op. at 39, n.21.

CONCLUSION

For the reasons set forth above, MCI respectfully requests that NARUC's Petition for Certiorari be denied.

Respectfully submitted,

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August 17, 1984

No. 84-95

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS,

Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF OF BELL OPERATING COMPANY RESPONDENTS IN OPPOSITION

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF OF BELL OPERATING COMPANY RESPONDENTS IN OPPOSITION

The Bell Operating Companies,[1] intervenors in support of the Federal Communications Commission in the Court

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[1]The following companies join in this Brief: Illinois Bell Telephone Company, Indiana Bell Telephone Company, Inc., Michigan Bell Telephone Company, The Ohio Bell Telephone Company, Wisconsin Telephone Company, New Jersey Bell Telephone Company, The Bell Telephone Company of Pennsylvania, The Chesapeake and Potomac Telephone Company, The Chesapeake and Potomac Telephone Company of Maryland, The Chesapeake and Potomac Telephone Company of Virginia, The Chesapeake and Potomac Telephone Company of West Virginia, The Diamond State Telephone Company, South Central Bell Telephone Company, Southern Bell Telephone and Telegraph Company, New York Telephone Company, New England Telephone and Telegraph Company, Pacific Bell, Nevada Bell and Southwestern Bell Telephone Company.

of Appeals for the District of Columbia Circuit below, and respondents here, submit this Brief in Opposition to the Petition of the National Association of Regulatory Utility Commissioners ("NARUC") for a Writ of Certiorari.[2]

COUNTERSTATEMENT OF THE CASE

NARUC seeks review of a unanimous decision of the D.C. Circuit Court of Appeals affirming the FCC's orders which establish a new, comprehensive system of interstate charges to recover the interstate costs of local telephone exchange facilities which furnish access to the nationwide telephone network. The petition challenges a single aspect

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[2]Illinois Bell Telephone Company, Indiana Bell Telephone Company, Michigan Bell Telephone Company, The Ohio Bell Telephone Company and Wisconsin Telephone Company are wholly owned subsidiaries of American Information Technologies Corporation, which has outstanding securities in the hands of the public. New Jersey Bell Telephone Company, The Bell Telephone Company of Pennsylvania, The Chesapeake and Potomac Telephone Company, The Chesapeake and Potomac Telephone Company of Maryland, The Chesapeake and Potomac Telephone Company of Virginia, The Chesapeake and Potomac Telphone Company of West Virginia and The Diamond State Telephone Company are wholly owned subsidiaries of Bell Atlantic Corporation, which has outstanding securities in the hands of the public. South Central Bell Telephone Company and Southern Bell Telephone and Telegraph Company are wholly owned subsidiaries of BellSouth Corporation, which has outstanding securities in the hands of the public. New York Telephone Company and New England Telephone and Telegraph Company are wholly owned subsidiaries of NYNEX Corporation, which has outstanding securities in the hands of the public. Pacific Bell and Nevada Bell are wholly owned subsidiaries of Pacific Telesis Group, which has outstanding securities in the hands of the public. Southwestern Bell Telephone Company is a wholly owned subsidiary of Southwestern Bell Corporation, which has outstanding securities in the hands of the public.

of that complex and multifaceted plan, the imposition of monthly flat end user charges upon telephone subscribers. The grounds of the petition are twofold: that the FCC's plan, as affirmed by the decision of the Court below, (1) conflicts with this Court's decision in *Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133 (1930), and (2) exceeds the FCC's statutory authority and improperly intrudes into the sphere of regulation of intrastate communications reserved to the States. Neither argument has any substance.

The Commission's action and the Circuit Court's affirmance do not conflict with *Smith*, or with any other decision of this Court or of any other Circuit Court of Appeals. *Smith* dealt solely with the question of allocating the costs of local telephone facilities – which are used for both interstate and intrastate calls – between the interstate and intrastate jurisdictions. *Smith* did not require allocation of these costs to any discrete body of customers, and did not address the manner in which those costs are to be recovered, the sole issue in this proceeding. In the present case there is no issue with respect to the allocation of costs. NARUC does not challenge the allocation of costs between jurisdictions. Simply stated, *Smith* is irrelevant to this proceeding.

Moreover, the Commission's action was not only well within the established boundaries of its statutory jurisdiction to regulate interstate communications, it in no way impinges upon the jurisdiction of the States. The rates established by the Commission are *interstate* rates designed to recover *interstate* costs. The States remain free to establish intrastate rates to recover intrastate costs. Thus, the petition presents no unresolved issue of national importance. There is, in sum, no basis for review on certiorari.

A. Background

This case involves the FCC's orders establishing a method for the recovery — through charges to telephone subscribers and carriers — of the interstate portion of the costs incurred by local exchange telephone companies (*e.g.*, the C & P Telephone Company) in providing access to the telephone network.

The costs at issue include the costs of installing and maintaining the local "loop," including poles, wires, and cables, that connects each customer's premises to the local telephone company's central office. These costs are real economic costs — they include the costs of telephone pole repair and replacement, the maintenance of underground cable damaged by flooding or other causes, as well as depreciation. These costs have two critical features. First, they are not caused by telephone calling or usage by individual subscribers.[3] Because these costs do not vary with the number or frequency of calls made, they are described as non-traffic sensitive ("NTS"). Second, the same local facilities or "loop" are used for both intrastate calling and interstate calling. There is no separate set of poles and cables allotted to intrastate calls and to interstate calls. Because these local facilities are used for both intrastate and interstate calling, some allocation of costs between the two jurisdictions is required.

In accordance with Section 410(c) of the Communications Act of 1934, 47 U.S.C. §410(c), the costs of these jointly used facilities have been divided for ratemaking

[3]Telephone usage causes a different set of costs such as the installation of additional central office switches and long-distance circuits, needed because of increased customer calling. Those costs, denoted traffic-sensitive costs, are not involved in this case.

purposes between the intrastate and interstate regulatory jurisdictions through a process known as "jurisdictional separations." That portion of the total non-traffic sensitive costs, approximately 74%, assigned to the intrastate jurisdiction has been recovered through rates set by the state public utility commissions. The portion of the costs assigned to the interstate jurisdiction — approximately 26% — has been recovered by interstate rates under the jurisdiction of the FCC.

There is no dispute in this case about the proper method of allocation, or the amount allocated, or the jurisdictional classification, of costs. All parties agree that the costs at issue — the 26% assigned to interstate — are *interstate* costs and that the FCC has jurisdiction to determine how they are to be recovered by the local telephone companies. The basic question in this case is the determination of how these *interstate* costs are to be recovered.

For many years, these non-traffic sensitive interstate costs have been recovered through long-distance rates charged on a usage basis depending on time and distance (e.g., $1.75 for a three-minute call from New York to Los Angeles, with an additional charge for each minute thereafter). As a result of this usage-based rate structure, heavy users of interstate service pay many times the interstate portion of the costs of their own loops, while light long-distance callers — whose loops cost just as much to maintain — may pay only a small fraction of the interstate costs of their loops.[4]

[4]As a hypothetical example, if the local loop has average total NTS costs of $24 per month in depreciation and maintenance expenses and $6 of those costs is allocated to the interstate jurisdiction, then the total interstate costs to be collected from *two* customers, each with his own loop, are $12 per month. If costs are recovered solely on a per call

In addition to this cross subsidy situation — high-volume users subsidizing low-volume users — the interstate rate structure has for some time contained other anomalies. For example, certain types of interstate calls could be made without involving any allocation of joint local costs to interstate, *i.e.,* Foreign Exchange (FX) service, described by the Court of Appeals in its Opinion at p. 23 (Pet. App. 23a). Further, the entry into the long-distance market in 1974 of other common carriers ("OCCs") in competition with AT&T raised additional discrepancies and disparities in the interstate rate structure. Until 1978, OCCs (such as MCI) and their subscribers made no contribution to the non-traffic sensitive costs allocated to the interstate jurisdiction. In 1978, an interim arrangement was made under which the OCCs made payments to the local telephone companies for the use of non-traffic sensitive facilities, but at a level below those made by the existing interstate carrier.

The Commission recognized that an interstate rate structure with all of these differentials and cross-subsidies could not be maintained in a competitive communications environment in which customers were free to switch to low-cost carriers and could bypass local facilities alto-

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basis and one user makes 11 calls and the other makes only one, at the rate of $1 per call, the high-volume user will pay $11 ($5 more than his own $6 interstate costs), and the light user will pay only $1 (which is only one-sixth of the interstate costs he imposes on the local telephone company). In actuality, the discrepancy is often far greater. About 3% of the nation's business customers generate about 60% of overall business telephone revenue.

gether.[5] The restructuring of interstate rates to accommodate the new technological and economic realities of the telecommunications industry became an urgent necessity. The FCC saw the need to eliminate these discrepancies and to move toward equal treatment of all customers. The forces that compelled this action were intensified by the break-up of the Bell System, which became effective January 1, 1984.

B. The Commission's Access Charge Plan

In 1978, the Commission instituted its proceeding in Docket 78-72 entitled *MTS and WATS Market Structure* to deal with these issues. A fundamental purpose of the plan developed by the FCC was to shift the burden of costs to those who caused them and to eliminate the unfairness of existing methods of recovery of non-traffic sensitive costs.

The FCC issued five notices and supplemental notices of proposed rulemaking and weighed the comments of over 140 parties spread over tens of thousands of pages of the administrative record before issuing its 253-page *Access*

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[5]Under a usage-based rate structure, high volume users are given a strong, artificial incentive to "bypass" the local telephone network by building their own communications facilities. As noted above, a very small percentage of customers generate most interstate revenues. For each telephone line, a heavy user may pay *each month* hundreds or even thousands of dollars as a contribution to interstate NTS costs through per call rates. Yet, the cost of that subscriber's NTS plant may be only $24 per month, of which only $6 has been allocated to interstate pursuant to Section 410(c) of the Communications Act. The high-volume user thus has a very strong incentive to bypass the network so long as he can do so at a cost less than the hundreds of thousands of dollars per month per line he is otherwise contributing.

Order, 93 F.C.C. 2d 241 (1983).[6] In reaching its decision, the FCC sought to accommodate four objectives: the continued assurance of universal telephone service, the elimination of unjust discrimination and unlawful preferential rates, the encouragement of network efficiency and the prevention of uneconomic bypass. The Commission concluded that these various objectives could best be met by a system of charges in which each residential and business telephone subscriber paid directly a flat monthly end user charge to cover most of the interstate, non-traffic sensitive costs of the plant dedicated to that subscriber.

The Commission's decision to impose a portion of the non-traffic sensitive costs upon all end users is both basically fair and in the overall public interest. It is fair because all end users cause those costs and in equity should pay for them. It is in the public interest because the FCC's approach would gradually phase out the subsidy of light users by heavy users, thereby lessening the threat of bypass and, at the same time, helping to preserve universal service.[7]

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[6]The *Access Order* was subsequently modified by the Commission's *Reconsideration Order,* 48 Fed.Reg. 42,984 (1983), and its *Further Reconsideration Order,* 49 Fed.Reg. 7,810 (1984) (which specifically addressed objections to the *Access Order*).

[7]The FCC found that this transition to end user charges should be achieved gradually, accompanied by a variety of measures designed to safeguard universal telephone service, including the creation of a Universal Service Fund to provide assistance to high cost exchange companies and the institution of proceedings to define a category of subscribers who would be exempt from the end user charge. Rather than collect the full interstate NTS costs at once through flat end user charges, the FCC's *Reconsideration Order* provided that in 1984, each residential end user would pay only $2 per month per line and each business user a maximum of $6 per month, with gradual increases in

Recovery of a portion of the non-traffic sensitive costs assigned to the interstate jurisdiction through flat end user charges also reduces the amount that must be recovered through other interstate charges.[8] The end user charges do not change the total amount of interstate costs associated with interstate service. They merely shift the mechanism of recovering those non-traffic sensitive costs from a usage charge to a flat charge basis.

C. Decision of The Court Below

On petitions for review by NARUC and others, the Court of Appeals for the District of Columbia Circuit affirmed in a lengthy *per curiam* opinion, 737 F.2d 1095. The Court concluded that "the decisions at issue, . . . are within the Commission's authority and, for the most part, are rationally grounded and sufficiently supported by evidence. We therefore affirm the FCC's orders in all major respects." (Pet. App. 19a).[9] The Court held that the FCC's decision to impose end user access charges for the recovery of interstate costs was within the Commission's statutory jurisdiction and did not conflict with this Court's decision in *Smith*. In the Court's view, the petitioner had misap-

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the following years. The Commission's *Further Reconsideration Order* further altered the imposition of end user charges, postponing until June 1, 1985 the implementation of end-user access charges for residential and single line business customers and placing a $4 ceiling on those charges until at least 1990.

[8]In addition to flat end user charges, the FCC imposed a monthly charge to be collected from interexchange carriers such as AT&T, GTE Sprint, MCI and SBS. This carrier common line charge is paid by the interexchange carriers as a contribution toward the recovery of the interstate allocation of NTS costs, separate and apart from the other charges paid by interexchange carriers to cover traffic sensitive switching and routing costs of local telephone companies.

[9]The Court remanded to the Commission two minor issues not pertinent to this proceeding. *Id.*

prehended the holding of *Smith* because *Smith* "did not address the manner in which the federal agency was to perform its task" of determining the method of recovery of those local telephone company costs assigned to the interstate jurisdiction. As the Court noted: "Petitioners confuse or blend two questions: (1) jurisdiction or authority to recover costs; (2) the manner in which costs are to be recovered." (Pet. App. 37a).

The Court further held that the Commission's decision to recover these costs through flat-rate end user charges did not exceed the Commission's statutory authority as limited by Section 2(b) of the Communications Act. In so holding, the Court focused on NARUC's fundamental misconception of the nature of the Commission's Order:

> Petitioners here lose sight of the Commission's main theme. The end user charge reflects costs caused not by a subscriber's actually making interstate calls, but by the subscriber's connection into the interstate network, which enables the subscriber to make interstate calls. The same loop that connects a telephone subscriber to the local exchange necessarily connects that subscriber into the interstate network as well. Under *Smith,* a portion of the costs of that loop are assigned to the interstate jurisdiction, for recovery under the regulatory authority of the FCC, on the basis of a complex division taking into account statistical calling patterns. That separations decision, however, does not affect the cost of the loop. Local telephone plant costs are real; they are necessarily incurred for each subscriber by virtue of the subscriber's interconnection into the local network, and they must be recovered regardless of how many or how few interstate calls (or local calls for that matter) a subscriber makes. The FCC may properly order

> recovery, through charges imposed on telephone subscribers, of the portion of those costs that, in accordance with *Smith,* have been placed in the interstate jurisdiction.

(Pet. App. 40a).

REASONS FOR DENYING THE WRIT

1. There Is No Conflict Between the Decision Below and This Court's Decision in *Smith v. Illinois Bell.*

NARUC seeks to create a ground for granting certiorari by fabricating an alleged conflict with *Smith v. Illinois Bell Telephone Company,* 282 U.S. 133 (1930). There is no conflict and NARUC's argument misstates both the holding and the implications of *Smith.*

The facts of the *Smith* case are detailed in the opinion of the Court of Appeals (Pet. App. 34a-37a) and there is no need to repeat them. The basic point is that *Smith* required only that a portion of the non-traffic sensitive costs of the local telephone loop be assigned to the interstate jurisdiction. *Smith* dealt solely with the requirement that the local exchange's non-traffic sensitive costs be apportioned, in some rough fashion,[10] between the interstate and the intrastate regulatory jurisdictions. *Smith* did not address how the two jurisdictions were to *recover* these costs. That is the fatal flaw in NARUC's argument. As the Court below carefully discussed, NARUC has improperly mixed

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[10]This Court recognized the difficulty of making such an apportionment, stating that "extreme nicety is not required, only reasonable measures being essential." 282 U.S. at 150. The only regulatory scheme ruled out by this Court in *Smith* was that with which it was faced, *i.e.*, one which "*ignore[d] altogether* the actual uses to which the property is put." *Id.* at 151. (Emphasis added).

the question of jurisdiction or authority to recover costs with the question of how those costs are to be recovered (Pet. App. 37a). *Smith* dealt only with jurisdiction. It did not deal with the manner of cost recovery.

NARUC's assertion that *Smith* requires that the cost of jointly-used local exchange property allocated to the interstate jurisdiction be recovered solely from "interstate end users" (or interstate carriers) is wrong for two reasons. First, *Smith* holds no such thing; it makes no reference to "interstate end users." As *Smith* recognized, the recovery of costs allocated to the interstate jurisdiction is the sole province of the federal regulatory agency. 282 U.S. at 148. The recovery of costs allocated to the intrastate jurisdiction is the sole province of the state regulatory agencies.

Second, the "interstate end user," who NARUC posits should bear the non-traffic sensitive costs allocated to the interstate jurisdiction, is a creature of NARUC's imagination. There is no separable class of "interstate end users." Although some telephone subscribers make many more interstate telephone calls than others and indeed, at certain time intervals, some subscribers may make no interstate calls, all subscribers are, in effect, "interstate end users" by virtue of the fact that their telephone is linked 24 hours a day, 365 days a year to the long distance, interstate, telephone network. Regardless of whether any given subscriber makes (or receives) a long distance call once a year or once a day, the same real economic costs of maintaining his or her access to the interstate network are incurred. Telephone poles must be repaired, and flooded or damaged cable must be replaced regardless of how often any given subscriber lifts the receiver to dial a call outside of his or her local exchange.

NARUC's suggestion that the interstate portion of non-traffic sensitive costs be recovered solely from a hypothetical class of "interstate users" also ignores the fact that when a telephone happens not to be used for interstate calls in a given month, an average of 26% of the non-traffic sensitive costs of that line are still assigned to the interstate jurisdiction. NARUC cannot have it both ways; because 26% of the non-traffic sensitive plant costs of each loop are assigned to the interstate jurisdiction, the structuring of rates to recover these interstate costs is a judgment reserved to the FCC.[11]

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[11]Section 410(c) of the Communications Act created a Federal/State Joint Board to make recommendations concerning the separation of non-traffic sensitive costs. 47 U.S.C. §410(c). NARUC argues that in enacting Section 410(c), Congress in effect endorsed NARUC's interpretation of *Smith*. NARUC's attempt to bolster its argument with fragments of the legislative history of Section 410(c) is unavailing. In enacting Section 410(c), Congress intended to *preserve* "federal superintendence" in the separations process. Senate Report No. 92-362 (September 17, 1971), reprinted in 2 U.S. Code Cong. & Adm. News (1971) at 1515 ("In order to retain *Federal superintendence* in this field, however, the State members [of the Joint Board] would not vote on the final decision. . . . H.R. 7048 would achieve the purpose of joint participation without abandoning *Federal superintendence* in the field"). (Emphasis added.)

An earlier version of the legislation would have given final authority over the separations process to the Joint Board. 117 Cong.Rec. 15981, 28906 (1971). As enacted, Section 410(c) gives the Joint Board advisory power only. The FCC retained final control over any cost allocation scheme. As one member of the House saw it, the legislation changed little, cost nothing and served "as a sop to the States." 117 Cong.Rec. 28907 (1971). Significantly, nothing in the legislative history suggests that Section 410(c) would have any bearing whatsoever on the manner in which the FCC provided for the *recovery* of costs allocated to the federal sector. The language which NARUC attributes to Senator Magnuson adds nothing to the debate. It is merely a paraphrase of the language of *Smith* itself, which requires cost separation, rather than a cost recovery mechanism.

2. The Access Charge Plan Was a Proper Exercise of the FCC's Jurisdiction Which Does Not Call For Intervention By This Court.

The FCC's access charge plan, including the end user charge, represents an ordinary and proper exercise of the Commission's jurisdiction to regulate interstate communications. The FCC's authority to regulate the matters in question is plain from the face of the Communications Act, and its decision to impose an end user charge is an exercise of discretion inappropriate for review by this Court on certiorari. Moreover, NARUC's legal arguments are grounded in a fundamental disagreement with the factual underpinnings of the decisions below. As NARUC frankly states, "NARUC does not agree with the D.C. Circuit's conclusion that a user incurs interstate costs merely by being provided with access to the interstate system regardless of whether he *ever* makes use of the system. Costs are incurred when a user accesses the system to originate and terminate interstate calls." (Petition at 18 n.20).

NARUC's petition suggests the kind of fact-specific inquiry which is plainly inappropriate for this Court's review on certiorari. The Court of Appeals concluded that, with two very narrow exceptions not pertinent here, the decision of the FCC was "rationally grounded and sufficiently supported by evidence" (Pet. App. at 19). These findings should not be reexamined.[12]

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[12] *Berenyi v. District Director, Immigration and Naturalization Service*, 385 U.S. 630, 635 (1967); *Graver Tank & Mfg. Co. v. Linde Air Products Co.*, 336 U.S. 271, 275 (1949). Denial of certiorari is further counseled by the principle that an agency's established construction of its enabling legislation and of the scope of its own jurisdiction is entitled to deference. See *Red Lion Broadcasting Co. v. FCC*, 395 U.S. 367 (1969); *North Carolina Utilities Comm'n v. FCC*, 552 F.2d 1036, 1043 (4th Cir. 1977), *cert. denied*, 434 U.S. 874 (1977) ("*North Carolina II*").

NARUC's claim that the FCC's end user access charge intrudes into the States' authority over "the intrastate sphere" bears no relationship to the facts underlying the FCC's exercise of its regulatory judgment. All non-traffic sensitive plant is in part *interstate* plant subject to FCC authority. Because the FCC's flat end user charges constitute a method of recovering *interstate* NTS costs which have been allocated to the *interstate* jurisdiction under statutory procedures, they are authorized under Section 2(a) of the Communications Act, 47 U.S.C. § 152(a).

Indeed, the FCC's action in the current case rests on much stronger ground than the earlier *North Carolina*[13] and *Computer II*[14] decisions, which were upheld by the Courts of Appeals and were denied certiorari.[15] This case

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[13]*North Carolina II; North Carolina Utilities Comm'n v. FCC,* 537 F.2d 787 (4th Cir.), *cert. denied,* 429 U.S. 1027 (1976) ("*North Carolina I*").

[14]*Computer and Communications Industry Ass'n v. FCC,* 693 F.2d 198 (D.C. Cir. 1982), *cert. denied,* 103 S.Ct. 2109 (1983) ("*Computer II*").

[15]Those cases upheld the federal power to preempt state regulation of customer premises equipment (i.e., telephone sets and other equipment on customers' premises), notwithstanding the fact that the principal use of that equipment was for intrastate communications. *See also, New York Tel. Co. v. FCC,* 631 F.2d 1059, 1062, 1064-66 (2d Cir. 1980) (FCC has jurisdiction over local exchange service when used in connection with interstate FX and CCSA services); *California v. FCC,* 567 F.2d 84, 86-87 (D.C. Cir. 1977), *cert. denied,* 434 U.S. 1010 (1978) (upholding FCC regulation of intrastate FX, given the impracticality of separating it from interstate FX); *Southern Pacific Communications Co. v. Corporation Comm'n,* 586 F.2d 327, 333 (Okla. 1978) (FCC's authority to regulate equipment used for both interstate and local communications is paramount even where the equipment is used predominantly for intrastate calls); *Puerto Rico Tel. Co. v. FCC,* 553 F.2d 694, 698-700 (1st Cir. 1977) (no matter how frequently or infrequently a subscriber places interstate calls, *federal* standards apply to conditions placed on access to interstate network).

is not a federal preemption case. There is no dispute here that the portion of the non-traffic sensitive costs assigned to the interstate jurisdiction are costs subject to the FCC's jurisdiction. This case simply concerns the exercise of federal jurisdiction over interstate rates about which there is no jurisdictional conflict.[16]

The *North Carolina* and *Computer II* cases are, however, instructive in establishing the limited application of Section 2(b) in restricting the FCC's exercise of its jurisdiction.[17]

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[16]*Pacific Gas & Electric Co. v. State Energy Resources Conservation and Development Commission,* ___ U.S. ___, 103 S.Ct. 1713, 75 L.Ed. 2d 752 (1983), cited by the Department of Public Utility Control of the State of Connecticut ("Connecticut") in its Brief in Support of NARUC's Petition, establishes no more than that the courts must respect and give effect to a statutory reservation of authority to the States. Neither that case, nor any of the arguments presented by Connecticut, in any way questions the fundamental proposition that the decision below was not based upon asserted preemption, nor upon a disregard for the reservation of authority to regulate intrastate communications to the States in Section 2(b). Rather, the decision below rests upon the proposition that the reservation of authority to the States did not prohibit the access charge in question here, because that charge is not an intrastate charge, but an interstate charge.

Connecticut's other argument in support of the petition is actually an attack upon the merits of the FCC's exercise of discretion to impose an end user access charge, rather than its jurisdiction to do so. That decision was a lawful and proper exercise of the Commission's decision making authority and was affirmed on that basis. (Pet. App. 44a-56a). In any event, this argument does not support the granting of a writ of certiorari to decide either of the questions presented by the NARUC petition.

[17]NARUC also refers to Section 221(b) of the Communications Act, 47 U.S.C. §221(b), as support for its argument that the FCC exceeded its authority in adopting an end user access charge. The Court of Appeals held "Section 221(b) is irrelevant to the problem before us; its limitation on Commission regulation of telephone exchange service was merely intended to preserve state regulation of local exchanges that happen to overlap state lines.' [*Computer II,* 693 F.2d at 216]." (Pet. App. at 39a n.21).

Section 2(b)(1), 47 U.S.C. §152(b)(1), which excludes intrastate communications from the Commission's regulatory authority, is applicable *only* to those intrastate facilities *"separable from* and . . . not substantially affect-[ing] the conduct or development of interstate communication." *North Carolina I,* 537 F.2d at 793. (Emphasis added.) The mere fact that facilities are used "predominantly" for local communication does not transform them into intrastate facilities for purposes of §2(b). *North Carolina II,* 552 F.2d at 1046.

The fact that end user charges may be imposed on some subscribers who elect to make no interstate calls is, contrary to NARUC's suggestion, without jurisdictional significance. As pointed out above, the charges are designed to recover costs that are incurred regardless of usage. Moreover, the decisions of the First, Second, Fourth and D.C. Circuits have established that the provisions of Section 2(b) of the Communications Act do not restrict the FCC's range of discretion in the exercise of its jurisdiction to regulate interstate communications. See n. 13-15, *supra.* As early as 1977, the Fourth Circuit characterized a similar attack on the FCC's jurisdiction as an "assault over old terrain." *North Carolina II,* 552 F.2d at 1044. As noted by the Court of Appeals in *North Carolina II,* it is "difficult to credit an argument which amounts to an assertion that Congress created a regulatory scheme that depends on the calling habits of telephone subscribers to determine the jurisdictional competence of the FCC versus state utility commissions." *Id.* at 1046. *See Computer II,* 693 F.2d at 214-17 (the mere fact that some telephone subscribers may use telephone equipment to make only local calls does not preclude the FCC from establishing policy relating to customer premises equipment).

The Fourth Circuit in *North Carolina II* specifically rejected an argument that the exercise of FCC jurisdiction

over terminal equipment would improperly deprive the States of meaningful ratemaking power by reducing opportunities for the state commissions to create subsidies for other services and facilities through revenues associated with terminal equipment. 552 F.2d at 1048. Like the equipment registration program sustained in *North Carolina II,* the Commission's access charge plan in no way purports to establish charges for local services; state commissions remain unfettered in their discretion to set rates for all local services and facilities provided by the telephone companies. 552 F.2d at 1047.

NARUC asserts that the *North Carolina* and *Computer II* cases, upon which the Court of Appeals relied below, are applicable only where the subject matter of regulation is inseparable between its interstate and intrastate aspects, such as a physically indivisible item of telephone terminal equipment. What NARUC overlooks is the fact that access to the interstate and intrastate networks, just like customer premises equipment, is in fact inseparable. Access to both the intrastate and interstate networks is automatically and necessarily conferred on *all* telephone subscribers.

NARUC's characterization of the end user charge as "an additional intrastate rate" is misleading and incorrect. (Petition at 17-18). The fact that payment of the end user charge may, as a practical matter, be a condition of local service merely reflects the inseparability of access to the local and interstate telephone networks. Where the FCC has lawfully established such a charge for interstate access, the fact that local service may incidentally be conditioned upon payment of such a charge does not make it an intrastate charge, and does not invalidate the FCC's action.

The FCC's access charge plan asserts jurisdiction only over the *interstate* costs of access to the network. As

NARUC notes, (Petition at 19-20), these costs have already been allocated to the interstate jurisdiction through the separations process. Therefore, there is no interference with state regulation of the recovery of intrastate costs, and no conflict between federal and state regulation that might require analysis under the principles of preemption.

Finally, the alternatives suggested by NARUC are, as the Court of Appeals pointed out, unworkable. (Pet. App. at 42-43). Adoption of NARUC's view that interstate access charges should be imposed only on those end users who actually make or receive interstate calls within a given billing period would involve the creation of an enormously complex and necessarily inefficient system for the allocation and collection of the relevant costs. The logical implication of such a policy, according to *Smith v. Illinois Bell,* would be to require an increase in the allocation of costs to be borne by the intrastate jurisdiction, and consequent recovery of those costs through increased intrastate rates charged by the operating companies to the "local" ratepayers. As the Court of Appeals noted, "it is hard to see what significant benefit NARUC would gain under such an arrangement." (Pet. App. at 43a).

Thus, the FCC's orders were well within the established bounds of the statutory authority of the Commission and do not conflict with the regulatory authority of the States. This case presents no unresolved issue of national importance that requires review by this Court.

CONCLUSION

For the foregoing reasons, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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DATED: September 19, 1984

No. 84-95

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

NATIONAL ASSOCIATION OF
REGULATORY UTILITY COMMISSIONERS,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION
and UNITED STATES OF AMERICA, *et al.,*
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF AMERICAN TELEPHONE AND TELEGRAPH COMPANY IN OPPOSITION

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RULE 28.1 LISTING

American Telephone and Telegraph Company, which has no parent company, retains a minority interest in two companies that have outstanding securities in the hands of the public[1]—Cincinnati Bell Inc. and The Southern New England Telephone Company.

[1] Counsel for AT&T understand Rule 28.1 to require disclosure of only those subsidiaries or affiliates with outstanding securities in the hands of the public.

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BRIEF OF AMERICAN TELEPHONE AND TELEGRAPH COMPANY IN OPPOSITION

Pursuant to Rule 22.1 of the Rules of this Court, respondent American Telephone and Telegraph Company ("AT&T") opposes the petition for certiorari filed by National Association of Regulatory Utility Commissioners ("NARUC").[1]

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[1] The time for filing this opposition was extended by the Court from August 20, 1984, to and including September 19, 1984.

STATEMENT OF THE CASE

This case concerns the way in which the Federal Communications Commission has structured interstate rates to recover from end users and interexchange carriers the interstate costs incurred by local telephone companies in originating and terminating interstate calls. The FCC adopted this rate structure after many years of study; interstate rates reflecting the FCC order have gone into effect; and the Court of Appeals has unanimously affirmed the agency on the basic issues presented below. NARUC's certiorari petition seeks review limited to one of those issues—the FCC's authority to recover fixed costs of the interstate telephone system from end users through fixed monthly charges.

1. A caller making or receiving telephone calls uses the same local telephone company facilities regardless of whether the calls are interstate or intrastate calls. Such calls travel over the same "loop" between the caller's home and the local telephone company switch at the local exchange, and the same switch at the exchange routes all such calls onward toward their destination. Most of the costs of these dual-use facilities—facilities used interchangeably for interstate and intrastate calls—are "non-traffic sensitive" costs; they are fixed costs that remain the same regardless of the number, length, or type of calls made.

Because these local telephone company facilities provide both interstate and intrastate service, responsibility for regulating rates designed to recover the costs of these facilities is divided between the FCC and state authorities. Under a formula developed pursuant to Section 410(c) of the Communications Act, 47 U.S.C. § 410(c), a portion of these local plant costs must be recovered through rates subject to the FCC's jurisdiction, and the balance through

rates subject to the jurisdiction of state authorities. Approximately 25% ($11 billion) of non-traffic sensitive local plant costs are assigned to the interstate jurisdiction for recovery through rates subject to the FCC's approval.

2. In this case, because of changes in the communications industry, the FCC fashioned a new approach for recovery of the portion of local telephone company plant costs assigned to its jurisdiction.[2] In the past, the non-traffic sensitive costs of a customer's line allocated to the interstate jurisdiction had been recovered on a per-call, usage sensitive basis; that is, a caller would pay for a portion of his line costs with every interstate call he made. Thus, an average-to-heavy user paid many times the cost of his local line while a light user paid little to none of the costs of his line allocated to the interstate jurisdiction. Under the FCC's new plan, the non-traffic sensitive customer line costs assigned to the FCC's jurisdiction will be recovered in part from telephone customers through flat monthly charges, thus ensuring that the interstate costs of a customer's line are borne by the actual cost causer.

Tariffs implementing the first phase of the FCC's new plan went into effect on May 25, 1984. A flat charge for multi-line business users is currently in effect at a rate of up to $6 per line. The remainder of the interstate non-traffic sensitive costs is now being paid by the long-distance carriers which in turn collect such amounts by charging their own customers. Residential and single-line business customers are scheduled to be assessed a flat rate starting in mid-1985. The initial amount of the rate has not yet been set finally, although the FCC has determined that it should not exceed $4 per line through 1990.[3]

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[2] The approach is set forth in a succession of FCC orders in 1983 and 1984 in the agency proceeding involved in this case. See Pet. App. 27a-32a. "Pet. App." refers to Appendix A to NARUC's petition.

[3] The FCC currently has underway proceedings to set these end user charges, providing such exemptions as may be needed to protect universal service.

3. On judicial review of the FCC's new plan, a number of parties mounted a variety of different challenges to the way in which the FCC had structured interstate rates in its new plan. Except in minor respects, the Court of Appeals rejected all of these challenges. The attack renewed here by NARUC does not challenge the reasonableness of the FCC's plan but rather the FCC's authority to direct the recovery of fixed interstate costs through fixed charges to be paid generally by telephone subscribers.[4]

NARUC claimed below and argues in this Court that the FCC-required fixed end user charge to recover the interstate costs in question conflicts with this Court's decision in *Smith* v. *Illinois Bell Telephone Co.*, 282 U.S. 133 (1930), and invades ratemaking authority reserved to the states by Section 2(b) of the Communications Act, 47 U.S.C. § 152(b). The Court of Appeals unanimously rejected these claims after a thorough analysis of the pertinent case law and arguments. In substance, the lower court found that *Smith* delineated the boundaries of state regulatory jurisdiction and has nothing to do with the FCC's choice among alternative interstate rate structures; and it rejected NARUC's Section 2(b) argument because

[4] The concerns prompting the FCC to adopt this approach included its desire to assure universal telephone service, achieve efficient use of the network, and assign responsibility for costs to those who cause them. In particular, the FCC was concerned that continuing the existing system, which requires heavy users to subsidize light users (see p. 3, above), was driving heavy users to "bypass" the network, leaving light users to make up the difference. A summary of the FCC's reasons appears in the opinion below (see Pet. App. 27a-32a); but detailed discussion is unnecessary because NARUC has not challenged the rationality of the FCC's action in this Court.

The Connecticut *amicus* brief claims that the access charges will impair universal service; but the court below specifically sustained the FCC's finding that most end users could afford to pay at least a portion of the cost of their own lines (Pet. App. 51a) and held that the FCC "had record support for the view that a charge could be imposed without substantial negative effect on universal service." *Id.* at 52a. The FCC found that usage-based charges (which drive heavy users to bypass the local network) pose a far greater threat to universal service than a system of fixed end user charges.

the FCC was engaged solely in structuring interstate rates to recover interstate costs.

SUMMARY OF ARGUMENT

Certiorari is not warranted in this case. See Sup. Ct. Rule 17. No conflict exists between this Court's decision in *Smith* v. *Illinois Bell Telephone Company,* 282 U.S. 133 (1930), and the FCC's decision to use fixed end user charges to recover the fixed costs assigned to the interstate jurisdiction. *Smith* delimited state-agency jurisdiction; by contrast, the FCC's action is simply the exercise of federal-agency authority to decide the structure of interstate rates.

Because the FCC's decision structures interstate rates to recover interstate costs, no invasion of state authority over intrastate rates is even remotely involved. No decision of this or any other court supports NARUC's reading of Section 2(b), 47 U.S.C. § 152(b), whereas the lower court's analysis is consistent with prior decisions in four circuits, which this Court has declined requests to review. See p. 10, n.11, below.

ARGUMENT

I. There Is No Conflict Between the Decision Below and *Smith.*

NARUC claims that the decision below conflicts with *Smith,* but it plainly does not. The Court in *Smith* decided that a state regulatory authority has no jurisdiction to set rates to recover costs attributable to interstate service.[5]

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[5] At issue in *Smith* was the validity of rates prescribed by the Illinois Commerce Commission for service provided by the Illinois Bell Telephone Company in Chicago. The telephone company attacked the rates as confiscatory, claiming that the allowed intrastate rate of return on its Chicago property was unlawfully low. The District Court agreed, but this Court

(footnote continues)

The Court held in *Smith* that a state agency may prescribe rates only for intrastate telephone service and that ratemaking for interstate service is the province of federal regulatory authorities. See pp. 8-10, below. This principle is carried out through the statutory mechanism by which costs of jointly used plant are assigned to the federal and state jurisdictions,[6] and each jurisdiction then takes responsibility for setting the rates to recover the costs assigned to it.

In this case, NARUC attacks the FCC's decision to recover, through the use of fixed end user charges, a portion of the fixed costs assigned to the interstate jurisdiction. However, nothing in *Smith* purported to decide *how* federal authorities may allocate among telephone customers the responsibility for paying costs assigned to the federal jurisdiction for recovery through interstate rates. See Pet. App. 37a-38a. *Smith* did not decide *who* should pay the costs of interstate telephone service; it simply decided that responsibility for setting rates to recover such costs belongs to federal authorities rather than the states.

(footnote continued)

reversed because interstate property had been included in the computations. The Court held that the company's rate base for state ratemaking purposes could include only that portion of the company's Chicago property devoted to intrastate service, and not the company's entire Chicago property. Accordingly, the Court directed the District Court to determine on remand whether the company's rate of return on that portion of its Chicago property devoted to intrastate service was lawful. Setting rates for interstate service was the province of federal regulatory authorities, the Court held, and telephone company property devoted to interstate service should not be included with property devoted to intrastate service in defining a telephone company's rate base for state ratemaking purposes—nor, as a result, for purposes of determining the validity of the state rates.

[6] See the discussion of Section 410(c) at pp. 2-3, above. The FCC's decision in this case did not change the pre-existing assignment formula; it concerned itself solely with the structure of interstate rates to recover those costs assigned to the interstate jurisdiction.

NARUC claims that the FCC's plan indirectly undermines *Smith* because allegedly its effect is to impose interstate costs on "local ratepayers." NARUC is mistaken in its premise that there exist "local ratepayers" who do not cause interstate costs. Each "local" customer's line provides access to interstate as well as intrastate service, and a portion of the cost of each customer's line is accordingly assigned to be recovered through interstate rates. Because the cost is non-traffic sensitive, it exists regardless of whether or how much the customer uses his line for interstate calls. All that the FCC has done here is to establish a system providing for partial recovery of such fixed costs through fixed monthly interstate charges to be paid by each customer, rather than continuing a system under which almost all such interstate costs were recovered on a per-call basis thus requiring heavy users to pay many times the cost of their own line. See p. 3, above.

By establishing a structure of interstate rates to recover interstate costs, the FCC has exercised the very federal authority that this Court recognized in *Smith* as belonging to the federal agency. See 282 U.S. at 148-49. As the Court of Appeals observed, "*Smith* dealt with jurisdiction; it . . . did not address the manner in which the federal agency was to perform its task." Pet. App. 37a. The reading of *Smith* advanced by NARUC is not supported by the language of *Smith*, its rationale, or any subsequent decision interpreting *Smith* either in this Court or in any other Court of Appeals. There is no warrant for further review.

II. In Establishing Its System of End User Interstate Charges To Recover Interstate Costs, the FCC Clearly Did Not Invade Regulatory Authority Reserved to the States.

NARUC also claims that the FCC's plan invades a sphere of ratemaking authority reserved to the states by the Communications Act. It relies primarily upon Section 2(b) of the Communications Act, 47 U.S.C. § 152(b), which restricts the FCC's jurisdiction over intrastate rates and services.[7] As the court below correctly held, neither Section 2(b), nor any other provision of the Act,[8] is infringed by the FCC's action.

In this case, the fixed end user charges adopted by the FCC are *interstate* rates limited to recovering costs assigned to the *interstate* jurisdiction. The FCC's rates do not recover costs assigned to the intrastate jurisdiction; those costs are recovered through rates established by state agencies, which are not at issue in this case. The FCC has exercised its own jurisdiction to set interstate rates and no infringement of state authority over intrastate rates is involved.

NARUC insists, however, that the FCC has *in effect* invaded state ratemaking jurisdiction by prescribing rates that function as a "precondition" of intrastate service. NARUC pet. 17. If subscribers must pay interstate rates

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[7] This limitation is itself subject, as the Courts of Appeals have held, to the FCC's overriding power to preempt state law to effectuate the purposes of the Act. See p. 10, n.11, below.

[8] NARUC also cites Section 221(b) of the Communications Act, 47 U.S.C. § 221(b), but it has no bearing on this case. Section 221(b) has been uniformly construed as limited to preserving state regulation of local exchanges that happen to overlap state lines. See, *e.g.*, *Computer and Communications Industry Association* v. *FCC*, 693 F.2d 198, 216-17 (D.C. Cir. 1982), *cert. denied*, 103 S. Ct. 2109 (1983). As the Court of Appeals concluded, "Section 221(b) is irrelevant" to the issue of the FCC's authority to prescribe the rates challenged by NARUC. Pet. App. 39a n.21.

in order to make intrastate calls, NARUC argues, then the interstate rates "amount to" additional intrastate charges (NARUC pet. 18), even though the rates are filed with the FCC as interstate rates and even though they recover interstate costs caused by the customer. NARUC's argument is mere rhetoric.

Interstate and intrastate service are interdependent not because of FCC regulation but because of technology. Because the same fixed customer line is used to originate and terminate local and long distance calls, and because a portion of the cost of that line is therefore allocated to the interstate jurisdiction and does not vary with the amount of use, the customer causes both interstate and intrastate costs when he or she subscribes to telephone service. The FCC's fixed end user charges simply recover from the customer a part of the *interstate* share of the costs of such dual-use facilities, and it cannot invade the state's jurisdiction for the FCC to insist that those interstate costs be paid by the customer.[9]

NARUC complains that interstate costs are being recovered from some customers who may make or receive no interstate calls in a given month. As the court below stated, this complaint might make sense "if a subscriber's choice not to make interstate calls meant that certain fixed 'interstate' costs would not be incurred." Pet. App. 42a. However, as the court below explained, "[a] subscriber's choice not to make or receive interstate calls . . . would not reduce the costs of that subscriber's loop; the local telephone plant costs would remain unchanged, as would the

[9] If NARUC's precondition argument had any substance, which it does not, it would as readily invalidate an entire body of state-regulated fixed charges for local monthly service that have been imposed for years in many jurisdictions. Paying those state-regulated charges could easily be described as a "precondition" of using the same home or business telephone for interstate service, a subject that Section 2(a) of the Act, 47 U.S.C. § 152(a), reserves to the FCC.

need to recover those costs." *Id.* at 43a. The court continued:

> "If we indulged NARUC's claim—that jurisdictional significance attends an individual subscriber's decision to use its line entirely for intrastate calls—then, as NARUC's counsel conceded, NARUC could hardly contest an allocation of all of such a subscriber's line costs (previously divided between the interstate and intrastate domains) to the intrastate jurisdiction alone. . . . It is hard to see what significant benefit NARUC would gain under such an arrangement." *Id.* (footnote omitted).[10]

NARUC does not claim that any decision of this Court or any other Court of Appeals supports its reading of Section 2(b). On the contrary, its petition (pp. 18-20) seeks to *distinguish* a consistent line of Court of Appeals decisions, representing the views of four circuits,[11] that the FCC *can* preempt state regulation where necessary to achieve federal ends. In this case the FCC's end user charges do not regulate intrastate rates or service, and no assertion of preemptive power is necessary to support the

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[10] To the extent that NARUC disagrees with the FCC's view that a customer imposes interstate costs by subscribing to telephone service (see Pet. 18 n.20), NARUC is arguing its theory of cost-causation in the wrong forum. The FCC concluded after five years of deliberation that sound policy required attributing to each subscriber the fixed cost of his connection to the network so far as that cost has been allocated to the interstate jurisdiction. The Court of Appeals accepted the FCC's judgment as rationally supported (see Pet. App. 42a) and this issue is hardly one meriting Supreme Court review.

[11] NARUC pet. 18 cites *North Carolina Utilities Comm'n* v. *FCC*, 537 F.2d 787 (4th Cir.), *cert. denied*, 429 U.S. 1027 (1976), *North Carolina Utilities Comm'n* v. *FCC*, 552 F.2d 1036 (4th Cir.), *cert. denied*, 434 U.S. 874 (1977), and *Computer and Communications Industry Association* v. *FCC*, *supra*. In addition, in cases not cited by NARUC, the First and Second Circuits have taken the same view. See *Puerto Rico Tel. Co.* v. *FCC*, 553 F.2d 694 (1st Cir. 1977); *New York Tel. Co.* v. *FCC*, 631 F.2d 1059 (2d Cir. 1980).

FCC's action here. The cases NARUC attacks merely illustrate how far *beyond* the FCC's action in the present case the agency may legitimately go to implement the policies of the Communications Act.

CONCLUSION

The decision of the Court of Appeals does not merit review under this Court's standards. See Sup. Ct. Rule 17. It is not in conflict with *Smith* or any other decision of this Court or any other Court of Appeals; and it does not involve any invasion of ratemaking authority reserved by the Communications Act to the states. For the foregoing reasons, the petition should be denied.

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September 19, 1984

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No. 84-95

In The
Supreme Court of the United States
October Term, 1984

National Association of
Regulatory Utility Commissioners,
Petitioner,
v.

Federal Communications Commission and
United States of America, *et al.*
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On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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BRIEF IN OPPOSITION OF RESPONDENTS THE MOUNTAIN STATES TELEPHONE AND TELEGRAPH COMPANY, NORTHWESTERN BELL TELEPHONE COMPANY AND PACIFIC NORTHWEST BELL TELEPHONE COMPANY

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BRIEF IN OPPOSITION OF RESPONDENTS THE MOUNTAIN STATES TELEPHONE AND TELEGRAPH COMPANY, NORTHWESTERN BELL TELEPHONE COMPANY AND PACIFIC NORTHWEST BELL TELEPHONE COMPANY

The Mountain States Telephone and Telegraph Company, Northwestern Bell Telephone Company and Pacific Northwest Bell Telephone Company[1] herewith sub-

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[1] The Mountain States Telephone and Telegraph Company, Northwestern Bell Telephone Company and Pacific Northwest Bell Telephone Company are three operating companies divested from AT&T

mit their brief in opposition to the petition for a writ of certiorari filed herein by the National Association of Regulatory Utility Commissioners ("NARUC").

STATEMENT OF THE CASE

Responding to fundamental and dynamic changes in the telecommunications industry—a technological revolution and the break-up of AT&T, which, until January 1, 1984, provided most long-distance and local exchange telephone services on a unified basis—the Federal Communications Commission ("Commission") issued a historic order on February 28, 1983, in which it prescribed, *inter alia*, a new method of cost recovery for that portion of local telephone company plant and equipment allocable to interstate services.[2] This order was preceded by over five years of extensive and intensive study by the Commission, including the solicitation and consideration of the views, proposals and arguments of every facet of the telecommunications industry.[3] The Access Order was followed by two further pronouncements of the Commission which fine-tuned and modified many of the provisions of the original order.[4] In review of the foregoing administrative action, the Court of Appeals for

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under the *Modified Final Judgment* in *United States v. AT&T*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983) (*"MFJ"*). These operating companies provide exchange telecommunications and exchange access services within fourteen states. All of the outstanding stock in these companies is owned by U S West, Inc., an individual holding company established pursuant to the *MFJ*.

[2] *MTS and WATS Market Structure: Third Report and Order*, 93 FCC 2d 241 (1983) ("Access Order").

[3] *See NARUC v. FCC*, No. 83-1225, slip op. at 109 (D.C. Cir. June 12, 1984).

[4] *MTS and WATS Market Structure: Memorandum Opinion and Order*, 48 Fed. Reg. 42984 (1983) (Reconsideration Order), 49 Fed. Reg. 7810 (1984) (Further Reconsideration Order).

the District of Columbia Circuit found that the Commission's action was "rationally grounded and sufficiently supported by evidence." [5]

One of the principal determinations made by the Commission in its Access Order (and the focus of the instant petition for a writ of certiorari) was that part of the cost of local telephone company plant used in interstate services should be recovered through a system of flat fees assessed against all telephone subscribers. This flat end-user fee (initially denominated the "Customer Access Line Charge" or "CALC") is calculated to recover a portion of the cost of nontraffic-sensitive plant utilized to provide access to the interstate network.[6] Specifically, these interstate costs are a portion of the nontraffic-sensitive costs which must be incurred to connect a customer to both the local network and the long-distance network (*e.g.*, the wire between the customer's premises and the local exchange central office), which are assigned to the jurisdiction of the Commission by a process known as "separations." [7] Because the plant costs themselves

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[5] *NARUC v. FCC*, slip op. at 19. In a brief supporting the NARUC Petition, the Connecticut Department of Public Utility Control argues that there was an insufficient evidentiary basis for the Commission's action. However, once a court of appeals has determined that an agency factual decision is supported by substantial evidence, the case does not merit further review. *NLRB v. Pittsburgh S. S. Co.*, 340 U.S. 498, 502-03 (1951).

[6] *See NARUC v. FCC*, slip op. at 29. NTS costs, in turn, constitute a large part of the cost of the local telephone plant. *Id.* at 19.

[7] Since this Court's decision in *Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133 (1930) (hereinafter "*Smith*"), the regulatory scheme for cost recovery of local telephone company facilities has provided for an allocation of such recovery between the federal regulator (originally the Interstate Commerce Commission, now the Federal Communications Commission) and the various state regulatory commissions. Under this format, an ascertainment was made of the portion of local telephone company facility costs attributable to the provision of interstate (long-distance) services, and that portion was recoverable through rates set by the federal regulator. The remaining cost recovery was the regulatory responsibility of

are nontraffic-sensitive, they do not vary with usage. For example, the cost of connecting a telephone subscriber's premises with the telephone network is the same whether the telephone is used not at all, infrequently, or non-stop.

While the Access Order did not modify the manner in which a portion of nontraffic-sensitive plant costs was allocated to the interstate (*i.e.*, the Commission's) jurisdiction, it *did* modify the manner in which the costs thus allocated would be recovered from customers. Before issuance of the Access Order, recovery of local plant costs allocated to the interstate jurisdiction was obtained through usage-based charges imposed on the makers of long-distance calls. It is conceded that this system subjected "heavy long-distance users" to payment of a disproportionate part of NTS costs of local facilities.[8] Maintenance of that recovery system also had the potential, according to the Commission's studies and its own expert analysis, of leading to the development of less efficient alternatives through use of "bypass" technologies and the abandonment of the local telephone network by heavy interstate users.[9]

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the various state agencies. Prior to *Smith,* there had been an informal division of long-distance toll revenues between the long-distance supplier (AT&T) and the local telephone company (*e.g.*, Illinois Bell). *See Smith,* 282 U.S. at 143; *Houston v. Southwestern Bell Tel. Co.*, 259 U.S. 318, 322 (1922); *Illinois Bell Tel. Co. v. Moynihan,* 38 F.2d 77, 83 (N.D. Ill.), *rev'd sub nom. Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133 (1930).

[8] *See NARUC v. FCC,* slip op. at 22.

[9] *See id.* at 29. In this context, bypass may occur when telecommunications suppliers are forced to price services in an uneconomic manner, thus driving customers to alternative suppliers. For example, traffic-sensitive pricing to recover nontraffic-sensitive costs will have the effect of causing heavy volume customers to seek suppliers whose prices are more reasonably related to the costs incurred in providing service.

In the exercise of its regulatory responsibility, the Commission concluded that a more realistic form of interstate telephone cost recovery was required in order to promote competition and avoid damage to the telephone network. Specifically, the Commission reasoned that all subscribers for use of plant used jointly for interstate and intrastate service should contribute to recovery of nontraffic-sensitive costs incurred on their behalf through payment of an end-user charge.[10] The balance of cost recovery for that portion of local telephone plant assigned to the interstate jurisdiction will continue to be funded, ultimately, from usage-based charges imposed on long-distance carriers and callers.

SUMMARY OF ARGUMENT

Under the doctrine announced in *Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133 (1930), there must be an allocation of those costs of the local telephone system which are attributable to use of the local exchange for the origination and termination of interstate services, and such costs are to be recovered in accordance with rules established by the federal regulator. This allocation of jurisdiction is reflective of the joint federal-state regulation of the telephone system, under which the federal regulator is responsible for regulation of interstate telecommunications and the various state commissions have regulatory authority over intrastate services. In cases in which the same plant is used for both interstate and intrastate services, *Smith* mandates a jurisdictional (as opposed to a physical) separation in order that both federal and state regulators may properly function in their respective domains.

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[10] Mindful of the impact of this ratemaking change, the Commission provided in its Access Order and in its subsequent reconsideration orders for deferral of imposition of the charge on residential and single-line business users, a maximum charge for such users through the year 1990 and other transitional measures. *See NARUC v. FCC,* slip op. at 31-32.

In its Access Order, the Commission honored the jurisdictional separation mandated by the *Smith* case. The Commission's determination that a portion of local telephone plant costs attributable to interstate services be recovered through a system of charges imposed on subscribers to the joint network was fully consistent with the *Smith* rationale. There is no conflict between the Commission's action and any decision of this Court.

The instant petition raises no other question worthy of this Court's review. Indeed, the record shows that the Commission acted within the scope of its regulatory authority, that its decision is supported by substantial evidence, and that whatever further refinements should be made in this field are best left to the federal regulator. The principal question here is one of regulatory policy, and that is an area traditionally and wisely reserved to the cognizant federal agency.

ARGUMENT

I. THE COMMISSION'S ACTION WAS FULLY CONSONANT WITH *SMITH v. ILLINOIS BELL*

NARUC, relying almost entirely on *Smith*, asserts that the Access Order is illegal and should be reversed. It is NARUC's position that *Smith* mandates that the Commission must direct recovery of nontraffic-sensitive exchange costs assigned to the interstate jurisdiction in a manner which is based upon actual usage of the interstate network (*i.e.*, on a traffic-sensitive basis). Contrary to NARUC's assertion, the essence of *Smith* is jurisdictional separation, not tariff structure. That essence appears clearly from the language of the *Smith* opinion; it is apparent as well in this Court's consistent statements concerning the *Smith* rationale. Simply stated, *Smith* requires that a part of the recovery of local exchange costs be assigned to the jurisdiction of the Commission. *Smith* does not in any way limit or delineate the type of interstate tariff structure which

should govern those rates once they have been validly assigned to the Commission's jurisdiction.

The jurisdictional nature of *Smith* is apparent from other contemporaneous decisions of this Court. For example, it was observed in *Wabash Valley Electric Co. v. Young*, 287 U.S. 488, 497-98 (1933) that under *Smith*:

> where the business of a carrier or utility is both interstate and intrastate, the state rates for intrastate transportation or business must be determined by a separate consideration of the value of the property employed in the intrastate business.

This Court stressed the jurisdictional nature of the separation process announced in *Smith* by noting that separation was required "because a different government exercises the ratemaking power in each of the two fields of regulation . . . ."[11] Likewise, in *Lindheimer v. Illinois Bell Telephone Co.*, 292 U.S. 151 (1934) (when the *Smith* litigation returned to this Court for the second time), the earlier holding was characterized as follows: "We found that separation was essential to the appropriate recognition of the competent governmental authority in each field of regulation."[12]

Thus, the *Smith* decisional rule is that proper ratemaking methodology requires that the exercise of the ratemaking power be confined to the property, revenues and costs within the jurisdictional authority of the ratemaker. In the telephone/telecommunications field, this translates into a rule that the various state commissions have ratemaking authority over intrastate services and the plant associated with those services, while the Com-

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[11] *Wabash Valley Electric*, 287 U.S. at 498.

[12] *Lindheimer*, 292 U.S. at 155. *See also Lone Star Gas Co. v. Texas*, 304 U.S. 224, 241 (1938) where *Smith* was described as "a case where the segregation of properties and business was essential in order to confine the exercise of state power to its own proper province."

mission has sole ratemaking authority over interstate plant and services.[13] The Access Order does not represent or constitute a breach of that regulatory demarcation. All the Commission has done is devise a method for recovery of the NTS portion of local plant costs assigned to its jurisdiction. While the flat rate method of such recovery is new, it is nevertheless in full compliance with *Smith*.

NARUC, while asserting that the Access Order is inconsistent with the *Smith* rationale, concedes that *Smith*: (i) does not require any particular method of cost recovery;[14] (ii) does not specify that cost recovery be on an usage-sensitive basis; and (iii) does not hold that cost recovery must be from long-distance carriers.[15] NARUC further concedes that *any* method which provides for cost recovery from the interstate jurisdiction is proper under *Smith*. Nonetheless, NARUC argues, inexplicably and without citation of authority, that the Commission has impermissibly transferred all local plant costs to the intrastate jurisdiction, thus creating an alleged conflict with *Smith*.[16]

NARUC premises its argument on two principal points: (i) the asserted existence of two distinct and

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[13] The jurisdictional separation mandated by *Smith* militates against the regulatory whipsawing of public utilities by the two ratemaking jurisdictions. The Court stated it thus in *Smith*: "The [State] Commission would have had no authority to impose intrastate rates, if as such they would be confiscatory, on the theory that the interstate revenue of the Company was too small and could be increased to make good the loss." 282 U.S. at 148-49. *See also New York Telephone Co. v. FCC*, 631 F.2d 1059 (2d Cir. 1980).

[14] Indeed, *Smith* does not deal with this subject at all.

[15] *See* NARUC Petition at 13. In actuality, interstate charges assessed against long-distance carriers are ultimately paid by telephone subscribers, through toll charges and the like.

[16] It is noteworthy that the Connecticut Department of Public Utility Control makes no such contention in its supporting brief.

separable classes of telephone ratepayers, intrastate and interstate; and (ii) the fact that all telephone subscribers must pay the new access charge in order to obtain telephone service.[17] Based upon these two considerations, NARUC asserts that the end-user charges required by the Commission constitute intrastate charges in violation of *Smith*. Both of these premises are ill-founded.

Initially, nowhere in *Smith* can be found any reference to the two distinct classes of telephone ratepayers imagined by NARUC. What the Court dealt with in *Smith* was the existence of two regulatory authorities over telephone service and the need to define and respect the jurisdictional limits of each. In fact, there is only one kind of telephone user, namely the subscriber to the present telephone system, which provides access to intrastate and interstate service jointly through common nontraffic-sensitive plant.[18] There is no basis in fact for the artificial segregation advanced by NARUC, nor does *Smith* anywhere provide a precedential basis for same.

NARUC further argues that *Smith* and Section 410(c) of the Communications Act,[19] allegedly codifying *Smith*, require that the interstate jurisdiction reimburse "the local system for the interstate system's use of its facilities."[20] In effect, however, that is exactly what is accomplished by the Access Order. Subscribers who utilize nontraffic-sensitive plant used to provide interstate service are to pay an access charge which is related to the attributed interstate costs of the local plant. This access

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[17] NARUC claims a constituency of telephone users who neither make nor receive interstate calls. This "class" is not otherwise defined.

[18] Every user of interstate telephone service is a local exchange ratepayer somewhere.

[19] 47 U.S.C. § 410(c) (1982).

[20] NARUC Petition at 15.

charge will be paid to the local telephone companies in reimbursement for interstate use of local facilities. *Smith* is thus followed in both letter and spirit.[21]

There is likewise no merit to the contention that, because the access charge plan requires payment of the interstate cost of the local exchange as a pre-condition to obtaining combined interstate and intrastate service, this somehow transforms the charge into an intrastate rate. This feature no more changes the jurisdictional nature of the charge than do the several state regulatory provisions requiring payment of local charges as a condition for receiving telephone service (which includes interstate services).

The access charge is one determined to be appropriate by the Commission, in the proper exercise of its regulatory authority, and is a charge which is required to be paid before access will be provided to the interstate system through use of exchange plant assigned to the interstate jurisdiction. This manner of payment for the interstate portion of jointly used plant in no way results in an unlawful incursion into the regulatory sphere of the state public utility commissions.

II. THE QUESTIONS RAISED IN THE PETITION ARE NOT OF COMPELLING IMPORTANCE

There being no conflict with the *Smith* requirements, the NARUC petition is devoid of issues meriting the attention of this Court. The argument that the Access Order must be invalidated for the benefit of an undefined class of telephone subscribers "who do not make any use of the interstate system and who, if given the choice, would choose to take intrastate-only access" clearly is

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[21] The principal thrust of the supporting brief filed by the Connecticut Department of Public Utility Control is that the access charge will adversely affect "universal service." This is contrary to the *factual* determination of the Commission which, upon review, was found to be supported by substantial evidence.

unworthy of consideration.[22] Putting aside the factual implausibility of this allegation, NARUC does not have the requisite standing to assert this claim,[23] and the claim lacks necessary definiteness and concreteness.[24]

This Court in particular, and the federal judiciary in general, do not sit as super-agencies in review of regulatory methodology. Once it has been established that basic legal requirements have been met and that the regulatory action is statutorily authorized, judicial review is at an end. In the instant case, the Commission determined, after lengthy and extensive deliberation and consideration, to revise the format for recovery of certain interstate costs of the local telephone system. In review, the court of appeals concluded that the action of the Commission was supported by substantial evidence and that the action otherwise was in accordance with law. Further judicial review is neither required nor warranted.

What NARUC is really seeking is that this Court order maintenance of the *status quo* with respect to the manner in which the interstate portion of local plant costs is recovered, notwithstanding the reasoned, expert determination of the Commission that technological and marketplace changes in the telecommunications industry dictated a regulatory change. The net effect of the NARUC position, notwithstanding its protestations to the contrary, is that cost recovery on a usage-sensitive basis is the only permissible method. NARUC's insistence that actual use of the interstate system is a jurisdictional pre-

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[22] NARUC Petition at 18 n.20. NARUC's demand that the Commission "must be required to make available intrastate-only telephone service" (*id.*) is addressed to the wrong party.

[23] *See Larson v. Valente*, 456 U.S. 228, 238-39 (1982); *Valley Forge Christian College v. Americans United for Separation of Church and State, Inc.*, 454 U.S. 464, 471 (1982).

[24] It has been repeatedly emphasized that this Court does not sit "to decide abstract, hypothetical or contingent questions . . . ." *Thorpe v. Housing Authority*, 393 U.S. 268, 284 (1969).

requisite for interstate cost recovery would necessarily limit cost recovery to a usage-basis methodology. The only other alternative would be individual ratemaking and it was found below that such a system of individual ratemaking "would be prohibitively complex and inefficient." [25] Further, the NARUC proposal would result in no net benefit to the consumer since recovery of all line costs would have to come from local rates.[26]

NARUC's attempt to distinguish the court of appeals rulings relied upon below is unavailing. NARUC asserts that those cases involved federal regulation of equipment that was "not feasibly separable for regulatory purposes," while the Access Order dealt with separable costs.[27] However, the cases cited by NARUC [28] dealt with federal preemption of state regulatory authority while, by contrast, in the Access Order the Commission was simply exercising its jurisdiction in the precise area mandated by *Smith*. Moreover, the so-called separable costs perceived by NARUC are for plant and equipment used for interstate *and* intrastate service at one and the same time. These costs are "not feasibly separable" with respect to access to the telephone system, and the rationale of the cases relied upon by the court of appeals is and was fully applicable here.

It is no more impermissible for the Commission to require that all subscribers to telephone service pay their fair share of the interstate cost of providing such serv-

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[25] *See NARUC v. FCC,* slip op. at 43 n.22.

[26] *See id.* at 43.

[27] NARUC Petition at 19.

[28] *See Computer and Communications Industry Ass'n v. FCC,* 693 F.2d 198 (D.C. Cir. 1982), *cert. denied,* 461 U.S. 938 (1983); *North Carolina Utilities Commission v. FCC,* 552 F.2d 1036 (4th Cir.), *cert. denied,* 434 U.S. 874 (1977); *North Carolina Utilities Commission v. FCC,* 537 F.2d 787 (4th Cir.), *cert. denied,* 429 U.S. 1027 (1976).

ice, regardless of use, than it is for the state commissions to assess charges for access to the local system, regardless of use. It is recognized that the solution developed by the Commission may not be a perfect one—but reasonableness, not perfection, is the standard for review.[29] The sensitivity of the Commission to the potential impact of the access charge plan is reflected by its determination to maintain an ongoing review of the effect thereof. The Commission will continue to provide a forum for the expression of concerns regarding the new cost-recovery system. The Commission has acted rationally and responsibly and within its regulatory powers. There is nothing for this Court to review.[30]

CONCLUSION

In the expert view of the Commission, the end-user access charge plan is necessary to assure the integrity and survival of the interstate telephone system. The Commission has concluded, again in the exercise of its expertise, that it is appropriate that *all* subscribers to that system pay a fair portion of the system's costs. The jurisdictional source for the Commission's decision is its unquestioned regulatory authority over interstate telephone services. The Commission's decision is directed to, and acts on, properties and revenues committed to its jurisdiction.

In devising a fair and reasonable structure for recovery of those nontraffic-sensitive costs which have been allocated to the interstate jurisdiction, the Commission properly limited its action in full compliance with the jurisdictional separation mandated by *Smith*. The Commission saw the need for a consistent and coherent national policy concerning the maintenance and enhance-

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[29] *See NARUC v. FCC, supra*, slip op. at 109.

[30] The Connecticut Department of Public Utility Control would have this Court set telecommunications *policy*, a role which this Court has traditionally declined.

ment of the interstate telephone system, and it acted accordingly. The Commission's action was otherwise well within the bounds of reasonableness. Thus, the instant petition raises no issue warranting exercise of this Court's *certiorari* discretion.

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September 19, 1984

No. 84-95

In the Supreme Court of the United States

OCTOBER TERM, 1984

NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS, PETITIONER

v.

FEDERAL COMMUNICATIONS COMMISSION AND UNITED STATES OF AMERICA, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENTS IN OPPOSITION

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QUESTIONS PRESENTED

This case raises questions as to the validity of certain aspects of the FCC's end-user access charge plan, which seeks to recover a part of the cost of local telephone company equipment. A large portion of that equipment is used for both intrastate and interstate service, and its cost is "non-traffic-sensitive" (does not vary with extent of use). The Commission has approved a plan pursuant to which most of the portion of these costs that is allocated to the "interstate jurisdiction" will be recovered through a flat access fee payable by all telephone subscribers, whether or not the particular subscriber makes interstate calls.

The questions presented are:

(1) Whether this end user access charge plan is inconsistent with *Smith* v. *Illinois Bell Telephone Co.*, 282 U.S. 133 (1930).

(2) Whether the Commission invaded the authority to set rates for intrastate service reserved to the states by the Communications Act.

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BRIEF FOR THE FEDERAL RESPONDENTS IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-110a) is reported at 737 F.2d 1095. The orders of the FCC are reported at 93 F.C.C. 2d 241, 48 Fed. Reg. 42984 (1983) (order on reconsideration), and 49 Fed. Reg. 7810 (1984) (order on further reconsideration).

JURISDICTION

The judgment of the court of appeals was entered on June 12, 1984. The petition for a writ of certiorari was filed on July 18, 1984. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. This case arises from a rulemaking proceeding undertaken by the Federal Communications Commission to determine how local telephone companies should recover

the "interstate" portion of the cost of those facilities that are used both for interstate and intrastate service. Interstate and intrastate telecommunications service customers use the same local exchange facilities to originate and terminate calls. Local calls, of course, use only the local exchange facilities. When a customer places a long-distance call, however, the call passes through the customer's local "loop" to the exchange "switch" of the local carrier. Only then is it routed through the equipment of a long-distance carrier. When the call reaches its destination city, it is again shunted into a local exchange and is routed to the local loop of the party being called. The effect of this arrangement — a product of the technical configuration of the system — is that part of the use, and thus part of the cost, of local telephone company equipment is attributable to interstate calling.

Pursuant to *Smith* v. *Illinois Bell Telephone Co.*, 282 U.S. 133 (1930), the costs associated with local exchange facilities must be apportioned between interstate and intrastate usage; jurisdiction is divided between the FCC and state public utilities commissions to regulate recovery of the respective shares. Pursuant to Section 410(c) of the Communications Act, 47 U.S.C. 410(c), the actual apportionment, known as the "separations process," is carried out by a board composed of state public utility commissioners and FCC commissioners, which prepares a recommended decision for review by the FCC. Once the "separations process" is carried out, the competent authority in each jurisdiction — *i.e.*, the FCC for the interstate share and the appropriate state public utilities commission for the intrastate share —determines how the share of costs subject to its jurisdiction is to be recovered.

A substantial component of the cost of local exchange facilities used for both interstate and intrastate service remains the same regardless of how much the facilities are

used, and indeed, whether or not they are used at all. This fixed cost component is known in the industry as "non-traffic sensitive" (NTS). Individual subscriber loops are responsible for the preponderance of NTS local exchange costs. Under the separations process the share of NTS local exchange costs allocated to interstate service (and thus subject to FCC jurisdiction) is currently approximately 26%. (Thus, about 26% of the cost of each subscriber's local loop could be deemed allocated to the interstate jurisdiction without regard to the subscriber's individual calling habits.)

The American Telephone & Telegraph Company (AT&T) traditionally has recovered most of the NTS local exchange costs subject to FCC jurisdiction through the familiar mechanism of long-distance toll charges: "usage-based charges imposed on the makers of long-distance calls" (Pet. App. 21a). AT&T in turn made appropriate transfer payments to local telephone companies. Under that recovery scheme, long-distance users bore the entire cost of the interstate portion of NTS costs, while telephone subscribers who made no long distance calls paid no part of the portion of the cost of these facilities that had been allocated to the interstate jurisdiction, even though the cost of these facilities did not vary with use.

2. Technological change and the emergence of firms wishing to compete with AT&T in the long-distance telephone service market impelled the FCC, beginning in 1978, to undertake a rulemaking proceeding to reexamine the basic market structure of the interstate telephone service industry (see Pet. App. 23a-25a). The Commission ultimately concluded that an open market structure and free competition in the interstate telecommunications industry would serve the public interest and further the goals of the Communications Act. *MTS & WATS Market Structure*

Inquiry, 81 F.C.C. 2d 177 (1980).[1] Then, in a series of orders generally known collectively as the "*Access Decision*," the Commission prescribed a comprehensive new system of charges to allow recovery of the interstate share of the cost of local exchange facilities. When the system becomes fully effective in 1990, most of the interstate portion of NTS local exchange costs will be recovered directly from telephone subscribers through a flat "access charge." The balance of the interstate NTS local exchange costs and most interstate service-attributable usage-sensitive local plant costs will be recovered by local operating companies from the interstate carriers through charges assessed on a usage basis. The interstate carriers will, in turn, defray these charges through the long-distance toll rates charged to their customers.[2]

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[1]The Commission's rulemaking proceeding was undertaken independently of the government's antitrust action that led to AT&T's divestiture of the local "Bell" operating companies effective January 1, 1984. By the time the Commission reached the issue of compensation for the interstate use of local facilities, however, the divestiture plan had been agreed to. That plan was a major aspect of the new competitive industry structure that the Commission considered in framing its *Access Decision*.

[2]On May 25, 1984, tariffs implementing the first phase of the Commission's plan became effective. Only multi-line business users now pay the end user charge; the Commission contemplates that an end user charge will be assessed to residential and single-line business customers within the next year. Pet. App. 31a-32a. The ultimate size of end user charges will be limited. In order to protect subscribers in areas with high fixed local plant costs, the Commission will permit a higher percentage of NTS costs in such areas to be allocated to the interstate jurisdiction, recovering the extra costs attributable to this "high cost factor" through usage-based charges to be levied on long-distance carriers and to be placed in a universal service fund. 93 F.C.C. 2d at 281-282. The FCC has initiated proceedings to determine the optimal level for end user charges that will further the goals of promoting an open market environment in the telecommunications industry while preserving universal service. As the court of appeals observed (Pet. App. 51a-52a) because the Commission has not determined the proper level of access charges, questions concerning their amount and any effect of their amount are premature.

3. Numerous petitions for review of the Commission's *Access Decision* were filed in the United States Court of Appeals for the District of Columbia Circuit. Many aspects of the Commission's ruling ranging far beyond the matters at issue here were challenged. The court of appeals affirmed the agency action in all but minor respects.

The court of appeals initially rejected petitioner's claim (renewed here) that *Smith* v. *Illinois Bell Telephone Co.* precludes imposition of a flat access charge on all telephone service subscribers. Describing petitioner's reading of *Smith* as "exorbitant" (Pet. App. 39a), the court of appeals explained that *Smith* held only that regulatory authority at the federal or state level must be addressed to the recovery of that share of local plant costs that is attributable to the class of service subject to its jurisdiction — *i.e.*, interstate and intrastate service, respectively. *Smith* requires that the cost of local plant equipment that is used in both intrastate and interstate service be apportioned between the two forms of service, and that this apportionment serve to demarcate federal and state jurisdiction. The fundamental flaw in petitioner's argument was identified by the court of appeals (Pet. App. 37a-38a; emphasis added):

> Petitioners confuse or blend two questions: (1) jurisdiction or authority to recover costs; (2) the manner in which costs are to be recovered. *Smith* dealt with jurisdiction; it held that a portion of the costs of local subscriber plant may be recovered only under the authority of a body with interstate regulatory powers. *The Smith Court did not address the manner in which the federal agency was to perform its task. It did not hold that the FCC must order recovery of costs allocated to its jurisdiction through usage-based charges.*

The court of appeals also rejected petitioner's contention that by imposing a flat rate access charge on all telephone subscribers the Commission had exceeded its jurisdiction

and had invaded the authority, reserved to the states by Section 2(b) of the Communications Act, 47 U.S.C. 152(b), to regulate intrastate telecommunication service (Pet. App. 39a-43a). The court held that the Commission has discretion to authorize recovery of the component of total NTS local plant costs allocated to FCC jurisdiction under *Smith* and 47 U.S.C. 410(c) through a flat user access charge paid by all telephone subscribers. The court observed that even though some subscribers may not make or receive any interstate calls, because the local plant costs defrayed by the access charge are non-usage sensitive, imposition of the charge on such subscribers is reasonable; the cost of local loop access recovered through the charge is not reduced by a subscriber's abstinence from use of the interstate service which the local loop makes available to him. The court noted that unless subscribers who make no interstate calls are simply to escape part of their share of NTS local plant costs, the alternative to use of a flat rate access charge paid by all subscribers would be to revise the separations process so as to make individualized allocations of the cost of local exchange equipment for each subscriber — a procedure that would be "prohibitively complex and inefficient" (Pet. App. 43a n.22). Thus, the court held, the Commission's approval of flat rate access charges does not amount to setting rates for intrastate service.

ARGUMENT

No question that warrants review by this Court is presented by the Commission's decision directing that a flat rate end user charge paid by all telephone subscribers be used to recover the interstate share of nontraffic sensitive costs of local exchange equipment used indivisibly for interstate and intrastate service.

1. a. Petitioner's contention (Pet. 8-16) that *Smith* v. *Illinois Bell Telephone Co.*, 282 U.S. 133 (1930), requires that interstate costs be borne entirely by those who place

interstate calls is wholly unfounded. As the court of appeals observed (Pet. App. 37a-38a), *Smith* addressed only the question whether the costs of the local exchange plant should be apportioned between interstate and intrastate service and jurisdictions; it did not discuss how — or from whom —those costs, once apportioned, are to be recovered. Indeed, petitioner has not identified any language in *Smith* that addresses the latter question and has not pointed to any subsequent authority that reads into *Smith* any directive concerning the recovery of costs allocated to interstate jurisdiction. Rather petitioner simply suggests that "*Smith* by its nature" requires the recovery of interstate jurisdictional costs from those who make interstate calls (Pet. 12). Petitioner appears to concede (Pet. 13, 16) that *Smith* would permit the FCC to impose flat end user charges on subscribers who actually make or receive interstate calls. But it contends that an access charge levied on all telephone subscribers because it is "a precondition to obtaining local service * * * amounts to an increase in intrastate rates" (Pet. 14).

Petitioner's argument is foreclosed by the separations process, which allocates to interstate service a portion of the cost of local exchange facilities capable of being used for both interstate and local calls. Regardless of his own calling habits, one who subscribes to local exchange service thus causes the local company to incur costs that are deemed interstate as a matter of law. Petitioner's challenge, then, is necessarily to the separations process itself — a matter outside the scope of this case.

Petitioner's argument, moreover, rests upon the incorrect assumption that local telephone service and long-distance service are severable and that a class of exclusively local telephone subscribers exists. But this dichotomy ignores the actual physical and technical properties of the telephone system. One who subscribes to local service

automatically secures access to interstate service — *i.e.*, the *capability* of making and receiving interstate calls.[3] A subscriber who chooses not to make interstate calls can still receive such calls. And because of the physical properties of the telephone system, such a subscriber would always be able to make or receive such calls in an emergency or simply because he changed his mind, without prearrangement. Thus it is reasonable to attribute to each subscriber the fixed costs of local plant equipment capable of being used for both interstate and local calls, whether or not the subscriber in fact makes use of interstate service, and to characterize part of this cost as a cost of making interstate service available to each such subscriber. Petitioner's contention that end user access charges are disguised intrastate rate increases accordingly is inaccurate.[4]

b. Petitioner contends (Pet. 14-16) that Section 410(c) of the Communications Act, 47 U.S.C. 410(c), and its legislative history show that Congress expected that the Joint Board created to carry out the apportionment process

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[3]Conversely, as we observed at the outset (page 2), one who wishes to place interstate calls must, because of the design of the system, ordinarily subscribe to local service.

[4]It is true, of course, that a subscriber who refuses to pay his "access" charge would be subject to termination of service, including local service. But that fact does not warrant characterization of the interstate access charge as an intrastate charge. It would be just as reasonable to characterize local exchange tariffs as a charge for interstate service, for payment for local service is a precondition to obtaining interstate service. But neither of these characterizations would be accurate; each is simply a reflection of the physical interconnection of interstate and local service. In fact, local tariffs recover intrastate costs, and the interstate rate (including the flat rate access charge for all subscribers) recovers interstate costs. In any event, even under the regime in effect prior to the *Access Decision*, local subscribers who refused to pay their long-distance bills were subject to termination of service. Thus the termination sanction does not establish that the access charge is a charge for local service.

required by *Smith* "would allocate costs to the interstate jurisdiction to be recovered in a way that would compensate the local system for the interstate system's use of its facilities" (Pet. 15). But petitioner has not suggested that the Commission's *Access Decision* will result in any failure to compensate local operating companies for the use of their facilities in making interstate calls. Nor would any such suggestion be tenable, for the access charge is designed to provide a means of recovering the amounts due to local carriers for interstate use of their facilities as determined in the separations process. The manner in which costs subject the FCC jurisdiction are recovered is a matter within the Commission's jurisdiction. Thus petitioner's argument based on Section 410(c) simply restates its contention that a flat rate access charge that extends to persons who do not make interstate calls is outside the Commission's jurisdiction. Nor does anything in the legislative history cited support petitioner's contention in this case. The legislative history of Section 410(c), like this Court's decision in *Smith*, addresses the apportionment of costs between the interstate and intrastate jurisdiction; it does not address the means by which either share is to be recovered.

c. Petitioner contends (Pet. 17-20) that the end user access charges prescribed by the Commission invade the authority over local rates reserved to the states by Sections 2(b) and 221(b) of the Communications Act, 47 U.S.C. 152(b) and 221(b). But the premise for this argument (by now familiar) is that the flat rate end user charge is effectively a charge for intrastate service because nonpayment will result in suspension of local service. As we have explained above (page 8 & note 4), this analysis based on the reach of sanctions for nonpayment of particular charges is misleading and ultimately indeterminate. Because of the physical properties of the telephone network, payment of local charges could as easily be said to be a precondition to

receiving long distance service. Petitioner's analysis leads to the untenable conclusion that *all charges* in the telephone system are both all interstate and all intrastate. Moreover, as we have explained, those who pay the access charge do in fact receive an important element of interstate service, whether or not they place or receive long distance calls, for they automatically secure access to the interstate system and acquire the capability to place or receive such calls without prearrangement. Because the interstate service share of costs defrayed through the access charge is comprised of nonusage-sensitive plant costs, it is entirely reasonable to regard the access charge as one that recovers costs attributable to interstate service.

In rejecting petitioner's claim that the access charge invades jurisdiction reserved to the states, the court below observed that the courts of appeals have upheld FCC regulation of practices — such as technical conditions upon which home telephones and answering machines may be connected to the telephone system — that necessarily affect both interstate and local service (Pet. App. 40a-42a, citing *North Carolina Utilities Commission* v. *FCC*, 552 F.2d 1036 (4th Cir.), cert. denied, 434 U.S. 874 (1977), and *Computer & Communications Industry Ass'n* v. *FCC*, 693 F.2d 198 (D.C. Cir. 1982), cert. denied, 461 U.S. 938 (1983)). Petitioner seeks to distinguish these earlier cases (Pet. 18-20), arguing that unlike rules for home telephone terminal equipment — which, in the nature of the system, must be uniform for interstate and local service — the interstate and intrastate shares of non-traffic sensitive local plant costs are susceptible to allocation. The allocability of these cost shares is wholly irrelevant here, however.

The flat rate access charge defrays only the interstate share of these costs as determined through the separations process. The Commission has made a permissible threshold

decision that non-usage sensitive local costs within its jurisdiction should generally be recovered by flat charges. The application of the access charge to persons who make no interstate calls — the nub of petitioner's complaint — then results from the superimposition of a divided jurisdictional scheme upon a physically unified telephone system no less than does the need for uniform rules governing equipment that may be connected to that system. As the court of appeals recognized (Pet. App. 42a-43a & n.22), unless the separations process were carried out in a highly burdensome individualized fashion, subscriber by subscriber, exempting persons who place no interstate calls from the access charge would give such persons an unwarranted subsidy. Fixed local plant costs have for many years been allocated pursuant to *Smith* and 47 U.S.C. 410(c) in a non-individualized manner. This history undercuts petitioner's argument, which would effectively require alteration of this practice. Compare Pet. 19-20.

2. Petitioner argues that the Court should grant certiorari because the case is of "critical national importance" (Pet. 17). The Commission recognizes that its decision mandating recovery of the interstate share of subscribers' line costs through flat rate charges imposed directly on end users is a significant change from the past practice. The Commission's decision is, however, entirely consistent with the broad principle that traditionally has informed public utility ratemaking: that rates should be determined on the basis of cost. See *FPC* v. *United Gas Pipe Line Co.*, 386 U.S. 237, 243 (1967); *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944). The Commission's ruling is also consistent with the corollary principle that costs generally should be recovered from the customer who is responsible for the utility's incurring them. See, *e.g., American Telephone & Telegraph Co.*, 61 F.C.C. 2d 587, 622 (1976), aff'd *sub nom. Aeronautical Radio, Inc.* v. *FCC*, 642 F.2d 1221

(D.C. Cir. 1980), cert. denied, 451 U.S. 920 (1981); *American Telephone & Telegraph Co.*, 64 F.C.C. 2d 1, 54-56 (1977). The Commission's decision rests on policy considerations that were carefully articulated and applied, and which flow directly from the Commission's central statutory mandate to make adequate service available nationwide, to ensure reasonable and nondiscriminatory charges, and to encourage more widespread and effective use of communications technologies. See 47 U.S.C. 151, 201-205, 218, 303(g).

Although cloaked in jurisdictional garb, petitioner's claim presents, in the final analysis, a challenge to the wisdom of the Commission's policy judgments. The critical issues in this case are, as the court of appeals recognized (Pet. App. 109a), matters for exercise of policy judgment. Expertise in such matters resides peculiarly in the political branches of government. *Chevron U.S.A., Inc.* v. *Natural Resources Defense Council, Inc.*, No. 82-1005 (June 25, 1984), slip op. 27-28. The Commission has exercised its judgment in this highly complex case in a manner that the court of appeals determined to be reasonable. In light of the character of the issues involved, any further review of the *Access Decision* should be at the hands of Congress. Recognizing the practical impact its decision might have, the Commission directed that it be implemented only after a transition period running through 1990. This transition period ensures that Congress will have an ample opportunity to review the Commission's ruling and to make any changes deemed appropriate by legislation. Congress is fully aware of the Commission's decision and has monitored the issues presented in this matter closely.[5]

[5]During the 98th Congress, 27 bills and resolutions have been introduced which would address aspects of the Commission's *Access Decision*. See S. 1382, S. 1626, S. 1660, S. 1667, S. 1830, S. 1931, S.J. Res. 151, H.R. 3364, H.R. 3365, H.R. 3440, H.R. 3522, H.R. 3569, H.R. 3602, H.R. 3621, H.R. 3647, H.R. 3671, H.R. 3809, H.R. 4102, H.R.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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OCTOBER 1984

4116, H.R. 4130, H.R. Con. Res. 150, H.R. Res. 231 (1st Sess., (1983)); S. Res. 308, S. Res. 353, H.R. Res. 4844, H.R. 6155, H.R. Res. 473 (2d Sess. (1984)). H.R. 4102 has passed the House of Representatives.

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No. 84-95

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1984

NATIONAL ASSOCIATION OF
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v.

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United States of America,
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BRIEF OF AMICUS CURIAE CITY OF LOS ANGELES IN SUPPORT OF PETITIONER NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS

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INTEREST OF AMICUS CURIAE

The City of Los Angeles ("Los Angeles"), a municipal corporation in the State of California, is deeply concerned with regard to the impact the imposition of an interstate access charge will have on Los Angeles ratepayers. Los Angeles has been very active for the last 25 years in California Public Utilities Commission ("CPUC") proceedings appearing on behalf of its citizen ratepayers as well as itself as a municipal corporation. It is in the interest of Los Angeles to ensure that the CPUC sets

reasonable rates which guarantee universal telephone service while concomitantly protecting the financial integrity of the telephone company. We believe that an identical interest is present in the case at bar because the interstate access charge will unreasonably increase costs for the local telephone ratepayers in California and in particular the City of Los Angeles.

Los Angeles supports the position of the National Association of Regulatory Utility Commissioners ("NARUC") in this proceeding. We file this brief to demonstrate our support and to stress several points which Los Angeles feels are critical to its citizen ratepayers.

STATEMENT OF THE CASE

The issue presented in this case evolved from the Federal Communication Commission's ("Commission") "Notice of Inquiry and Proposed Rulemaking" in the matter of MTS and WATS Market Structure, CC Docket No. 78-72 ("Notice of Inquiry"). Since the issuance of the Notice of Inquiry the Commission has issued several supplemental Notices of Inquiry and several Reports and Orders concerning this matter. Of particular concern to Los Angeles is the "Third Report and Order" released on February 28, 1983 and the "Memorandum Opinion and Order" released on August 22, 1983 (hereinafter referred to collectively as the "FCC Orders"); both deal, *inter alia,*with the imposition of interstate access charges on local end-users.

In the above referenced actions the Commission prescribed rules for calculating the charges that end-users will pay a local telephone company after December 31, 1983 for access to the interstate network. The FCC Orders call for the impositon of a flat charge for each residential or party line of $2.00 per month and for each

business line of $6.00 per month. In addition, the FCC Orders call for a transition period during which the residential end-users access charge would gradually increase to $4.00 per month. (Memorandum Opinion and Order, August 22, 1983, para. 33.) The access charge for the business end-users became effective June, 1984. The United States Court of Appeals for the District of Columbia Circuit upheld the FCC Orders with its decision issued June 12, 1984. (*NARUC v. FCC* (D.C. Cir. June 12, 1984) No. 83-1225 Slip Op.)

ARGUMENT

I.

THE INTERSTATE ACCESS CHARGE FOR NON-TRAFFIC SENSITIVE FACILITIES SHOULD BE IMPOSED UPON THE INTEREXCHANGE CARRIER

The purpose of the access charge is to compensate the local telephone companies for the use of their non-traffic sensitive ("NTS") facilities in the interstate market. Los Angeles agrees with this objective but disagrees with the way in which the Commission addressed the matter. The FCC Orders place the entire burden on the local telephone end-user. The unfortunate consequence of the FCC Orders occurs notwithstanding the fact that many end-users will not access the interstate network. The theory ostensibly is that the mere privilege of accessing the interstate market, irrespective of use, requires the imposition of an access charge. (*NARUC v. FCC* (D.C. Cir. June, 1984) No. 83-1225, Slip Opinion at p. 40.) The Court below agreed with the Commission and it denied the numerous petitions requesting the matter to be remanded.

Los Angeles believes that the FCC Orders are unfair and unlawful in several respects. First, many local end-

users will never use the interstate system and many that do will not use it very often. Such end-users are therefore paying for a service without a corresponding benefit. In other words, their property would be taken in violation of the compensation and Due Process Requirements of the Fifth and Fourteenth Amendments. (United States Constitution, Fifth and Fourteenth Amendments.) The beneficiaries of the FCC Orders are the interexchange carriers who will eventually pay nothing towards the costs of non-traffic sensitive plant but will reap huge profits from its use. By imposing such a charge the Commission exceeded its authority and is violating the Federal Communications Act of 1934 insofar as it is setting local intrastate telephone rates (47 U.S.C. 152(b)) rather than interstate rates (47 U.S.C. 201-205).

Los Angeles agrees with the NARUC position that *Smith v. Illinois Bell* (1930) 282 U.S. 133, does not mandate what formula should be utilized to make a fair apportionment, but it does mandate an apportionment. (NARUC Petition at pp. 13-14). The Court below likewise agrees on this point. The Court below erred, however, because it sustained the Commission position which allows the *entire* amount of NTS costs to eventually be placed on the local end-user. (*NARUC v. FCC*, *supra*, Slip Opinion at pp. 37-38.) It accepted the Commission position that the portion of NTS plant used in interstate calling should not be apportioned and thus limited apportionment to the local equipment used entirely for interstate calling (i.e. Common Carrier Line Access Equipment). In other words, where joint use of the same equipment exists no apportionment will be made. As NARUC states:

> "If the D.C. Circuit is correct and the FCC may recover these interstate costs from local exchange ratepayers, as it has attempted to do here, the result

would be the same as if *Smith* had never been decided. Local exchange ratepayers would bear all the costs of the jointly-used local facilities, as they had before 1930. The economic burden *Smith* was purposefully designed to eradicate would remain in full force." (NARUC Petition at p. 13.)

* * *

"The error in the D.C. Circuit's position is that it fails to accept the converse as true. If it is impermissible to allow the States to call for recovery of all local exchange plant costs from intrastate ratepayers it must also be improper to allow the FCC to do what amounts to the same thing by transferring all costs allocated to the interstate jurisdiction back to the intrastate jurisdiction for recovery through flat-rate end user access charges." (NARUC Petition at p. 14.)

The only fair way an apportionment can be made is to assess the interexchange carrier for that portion of the non-traffic sensitive plant that it uses. One method by which to achieve that result is to assign a cost, based upon minutes of use by interexchange customers, to the interexchange carrier. The interexchange carrier would then pass those costs on to its customers. Under this concept the user of the interstate system (i.e. the cost-causer) would be the party paying for the interstate portion of the non-traffic sensitive facilities. This is similar to the relative use concept adopted by the Commission in its April 16, 1980, "Second Supplemental Notice of Inquiry and Proposed Rulemaking." (In the matter of MTS and WATS Market Structure, CC Docket No. 78-72.) The Commission subsequently reversed that ruling with the adoption of the FCC Orders. Los Angeles respectfully

submits that the FCC Orders are an abuse of discretion and should be overturned.

Second, the purpose of the Communications Act of 1934 is to provide as near as possible "to all the people of the United States a rapid, efficient, Nationwide . . . wire and radio communications service . . . at reasonable prices" (47 U.S.C. 151(b)). With the above promulgation, Congress mandated universal telephone service at reasonable prices. The FCC Orders impose an access charge for non-traffic sensitive plant solely on the local end-user and thereby frustrate the purpose of the Act. The interstate access charge as contemplated will cause many subscribers to give up their telephones and "drop off the network", thus threatening the universal telephone service concept.

Although the Commission acknowledges that many subscribers may drop off the network it has not conducted any study to measure the adverse impact of its access charge order. Nationwide, the result could be in the millions and would threaten the health, welfare and safety of the public.[1] Such persons without telephone service would be unable to call the police, fire and medical authorities for help. If the Commission knew the actual number of subscribers that would drop off the system, it might change its mind with regard to the reasonableness of its orders.

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[1]In Application 83-06-65 a California Public Utilities Commission proceeding considering the imposition of an intrastate access charge. Pacific Telephone presented a study with findings that approximately 3% of its subscribers would drop off the network if California adopted a plan identical to that which the FCC has ordered. This estimate, which is conservative at best, means that approximately 240,000 subscribers in the State of California would drop off the network. Obviously, the number will be greater nationwide.

An important point not considered by the Commission is the consequences to the local end-user if the local telephone bill is paid but the interstate portion is not. For example, a situation may arise where a local end-user cannot afford to pay the entire bill and elects to pay only the local bill. Thus preserving the ability to call the police, fire and medical authorities for help. Will the local telephone company (at the order of the interstate company) terminate this customer's entire service or can the interstate service be blocked leaving the local access intact?

Such a situation exacerbates the FCC's intrusion into intrastate ratemaking. The Commission should provide a mechanism for terminating only the interstate service if a ratepayer fails to pay a long distance telephone bill. Under the current FCC Orders a local ratepayer will be denied the ability to make local calls if the ratepayer does not pay the interstate carrier for interstate service. Moreover, any arrangement whereby access to local telephone service is contingent upon payment for interstate service, violates the "Modified Final Judgment" which contemplates local operating companies which are independent from interstate carriers. (*United States v. AT & T* (D.D.C. 1982) 552 F. Supp. 131.) The Commission has not considered the proper methodology for the billing and termination of interstate services. Therefore, the FCC Orders should be vacated for that reason as well as others proffered by the petitioners in this proceeding.

II.

THE ACCESS CHARGE FOR CENTREX-CO USER SERVICE SHOULD BE RECONSIDERED

The Commission, with the FCC Orders, clarified its position with regard to the access charge to be imposed on the Centrex-Co user. Without analysis or reference to evidence in the record, it states that each Centrex line should be treated as any other line between a customer's

premises and the local switch that may be used for local exchange service and a variety of interexchange services. (In the matter of MTS and WATS Market Structure, CC Docket No. 78-72, Memorandum Opinion and Order, August 22, 1983, at Docket 78-72, para. 42.) However, a Centrex line is not like any other line and the Commission, as well as most other state commissions, has historically not treated Centrex the same as other lines for a variety of purposes (e.g., pricing). Indeed, the Commission's discussion in its Memorandum Opinion and Order (*supra*, at paragraphs 43-49) clearly points out the difference.

The Court below adopted in full the Commission's argument regarding the treatment of Centrex Co-User service. Both the Court and the Commission made reference to a record that allegedly supports its conclusions:

> "However, on the record before us we conclude that these arguments are without merit". (*NARUC v. FCC*, *supra*, at 58.)

The Court went on to state:

> "The Commission made other findings supported by record evidence which rationally buttressed its conclusion that there is no 'threat to universal service so substantial and so imminent that we must depart from this approach. . . .' Id. at 47, 49 Fed. Reg. at 7816." (*NARUC v. FCC*, *supra*, at p. 59.)

Yet, neither the Commission nor the Court make specific references to the portion of the record relied upon. Los Angeles submits that the record cannot support the conclusions by the Commission or the Court and that is why neither the FCC Orders nor the Court's Opinion contain specific references thereto. Accordingly, the order of the Court below should be reversed and the entire

matter remanded to the Commission for further hearings and the taking of evidence. To do otherwise will result in a hastily conceived and ill-considered conclusion which unjustifiably harms the ratepayers of this country.

CONCLUSION

On the basis of the foregoing, the City of Los Angeles respectfully submits that the FCC has abused its discretion and exceeded its authority with the adoption of the FCC Orders. The Opinion of the Court below is not supported by the record and should be reversed. The entire matter should be remanded for further consideration.

Dated:

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